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INDIAN
COMPANY LAW
AND
MANAGEMENT

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PREFACE

Industrialisation is the crying need of the hour, and the importance of the knowledge of Company Law in this age of industrialisation and planning cannot be over emphasized. The subject of Company Law has its own intricacies, which, what to say of a student, even a clever lawyer sometime finds it hard to follow. The principal object of this work is to present the subject in an easy and unconventional language free from technicalities. It is earnestly hoped that this book will serve as a reliable guide for the directors and other Company Officers, furnish the lawyers with just the ready and exact information for advising their clients, supply a real want for the ever increasing number of businessmen, in whose hands the control of the companies is almost universally placed, and will also help the students community preparing for advanced studies.

The present book is infact in continuation with my Commercial Law. It is submitted into three books—the First deals with Company Law, the Second, with the Philosophy and the Problems of Management and the Third, with Secretarial Practice.

A number of standard works have been consulted in the preparation of this book and I gratefully acknowledge the assistance received from them. My thanks are also due to Mrs. Lalita Saxena, who spared me from domestic worries and has enabled me to complete the work with patience.

I will welcome any suggestions that may be made from any quarter for the improvement of this book, which I shall thankfully incorporate in its next edition.

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BOOK ONE

Company Law



CONTAINING

Meaning of the term Company; Contribution and incorporation; Membership of Capitalisation; Call, Forfeiture; Surrender; Transfer and Transmission of shares; Borrowing powers and registration of mortgages; Contracts; Law relating to directors; Law relating to other company officers; Other company officers, Auditors; Law relating to holding and foreign companies and Winding up of Companies.



Company
stands for an association of a number of
persons for profit with capital
divisible into transferable shares
with limited liability, having a corporate
body and a common seal. — Lord Justice James.



CHAPTER I.

INTRODUCTION

MEANING OF THE TERM COMPANY

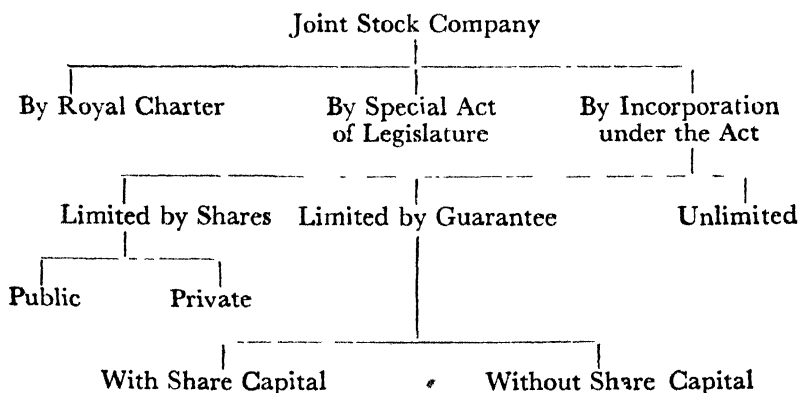
“ Ordinarily the term ‘company’ stands for an association of a number of persons for profit with capital divisible into transferable shares, with limited liability, having a corporate body and a common seal. Lord Justice James defined a ‘company’ in *Smith V Anderson*, 1880 (15 Ch. D. 247) as an association of persons united for a common object. Such an association may be in the form of an ordinary partnership or a Hindu Joint family business, or a society registered under the Societies Registration Act or a Provident Society or a Trade Union, or a company incorporated by Royal Charter or by an Act of Parliament or by some Indian Law, or it may be a company incorporated under the Indian Companies Act*. Section 2 (2) of the Indian Companies Act, 1913 has, however, narrowed down the Meaning of the term ‘company’ by stating that “company” means a company formed and registered under the Indian Companies Act, 1913, or an ‘existing company’ (which means a company formed and registered under the Indian Companies Act, 1866 or the Indian Companies Act, 1882). According to this definition, any organisation formed or registered under any of the Indian Companies Act can be called a company and none other. Further, Section 254 of the Act defines a joint stock company as “a company having a permanent paid up or nominal share capital of fixed amount divided into shares, also of fixed amount, or held and transferable as stock or dividend and held partly in one way and partly in the other, and formed on the principle of having for its members the holders of those shares or that stock, and no other persons.”

A company is a creation of law, and is sometimes called an artificial person endowed with a perpetual succession of members and an entity distinct from such members. A company is capable of holding property, incurring debts, and suing and being sued in the same manner as an individual. A shareholder cannot be held liable for the acts of the company. Unlike partners, the share-

holders cannot bind the company by their acts, because they are not its agents. Regarding the essential features of a 'company', Mr. M. C. Shukla beautifully writes in his "Indian Mercantile Law" as follows. "The legal personality and limited liability are the two important features of a company. It (company) has a right to sue and can be sued, but you cannot shake it by the hand, nor knock it down in a fit of temper. A company, being a cold abstract, artificial creature of the law, is distinct and separate from the flesh and blood of mortal men who from time to time comprise its members...the life of a company is independent of the lives of its members. Members may come and members may go, but the company goes on (until wound up). We are quite familiar with the expression. 'The King is dead; Long live the King !' That is just another way of saying that the crown has perpetual succession, i. e. the life of the crown is independent of the life of the individual king. In these respects the position of a shareholder in a company differs radically from that of a partner in a partnership business."*

KINDS OF COMPANIES

A Joint Stock Company may be formed in any of the following ways:—



1. **BY ROYAL CHARTER:**—Such kind of companies are floated with a view to exercise some prerogative of the crown, e. g., the government of a territory. The right to exercise these powers is given by the terms of the charter, and hence, such companies are sometimes known as, what we call "Chartered Companies." Examples of such companies are—The East India Company; The

Chartered Bank of India, Australia & China etc. etc. This Method of forming a company is now-a-days very rarely adopted.

2. **BY SPECIAL ACT OF LEGISLATURE:**—This Method of incorporation is followed for the purpose of carrying on some business of national importance, e. g., banking, transport etc. Such companies are known as “Statutory Companies”, and are exemplified by the Industrial Finance Corporation, The Reserve Bank of India etc.

Both the Chartered and the Statutory Companies are not required to use the word ‘limited’ as part of their names, even though the liability of their shareholders may be limited.

3. **BY INCORPORATION UNDER THE INDIAN COMPANIES ACT:**—This is the most popular method of incorporation or formation of companies. Such companies are known as “Incorporated” or “Registered” companies and are generally formed for trade and commerce. Except a few chartered and statutory companies, all existing companies in India belong to this category. As is clear from the above chart, Registered Companies may be (i) limited by shares, (ii) limited by guarantee or (iii) unlimited; and they may be public or private.

(I) **Company Limited by Shares:**—In a company limited by shares, the liability of the members is limited to the amount unpaid on their shares, i. e., they cannot be asked to contribute more than the face-value of the shares taken by them, irrespective of the amount of loss to the company.

(II) **Company Limited by Guarantee:**—It is a company in which the liability of its members is limited by the Memorandum of Association to such amount which they undertake to provide in the event of winding up. Companies limited by guarantee are either those having a share capital or those not having a share capital. In the Guarantee-companies having a share capital, each member is also liable for any amount remaining unpaid on his shares.

(III) **Unlimited Company:**—As is implied from the word ‘unlimited’, in unlimited liability companies, each member is liable for the debts of the company to the last pie. Such companies are practically non-existent.

Again, companies registered with limited liability both in England and India, may be Private Companies or Public Companies.

PRIVATE COMPANY:—Under Section 2 (1) clause 13, a private company is defined as a company which by its articles—

- (a) Restricts the right to transfer its shares;
- (b) Limits the number of its members to 50 (exclusive of present employees); and
- (c) Prohibits any invitation to the public to subscribe for its shares and debentures—

“Provided that where two or more persons hold one or more shares jointly, they shall be considered as single member.”

A private company is, therefore, required to send with its annual return (which is to be filed with the Registrar under Section 32) a certificate by an officer of the company that the company has not issued any invitation to the public to subscribe for any shares or debentures of the company. Since the membership of a private company is confined more or less to friends and relations, it enjoys certain special concessions, known as “Privileges” or “Legal Exemptions”, which are not allowed to the public company. These privileges are as follows:—

1. Only two signatories to the Memorandum of Association are sufficient in order to form a private company (Sec. 5).
2. A private company is not required to file a copy of the balance sheet or a statement in lieu of prospectus (Sec. 98).
3. It is not required to hold the Statutory Meeting or prepare the Statutory Report (Sec. 77).
4. It is not necessary that any of the directors of a private company should be subject to retirement by rotation (Sec. 83-B).
5. There is no restriction on the appointment and advertisement of the first directors of a private company (Sec. 84).
6. The Managing Agent of a private company may appoint more than $\frac{1}{3}$ of the total number of its directors (Sec. 87-1).
7. There are no restrictions on the allotment of shares by private company (Sec. 101).
8. There are no restrictions on the commencement in the case of a private company (Sec. 103). It can start business immediately on registration.

9. In the case of a private company, there is no need to circulate its accounts to the members, or to file them with the Registrar after they have been laid before the members at the Annual General Meeting (Sections 131 & 134).

10. Preference shareholders, etc., cannot inspect the audited accounts unless so permitted by the articles (Sec. 146).

11. The provisions regarding appointment of directors and regarding contracts by agents, do not apply, nor the new provisions of the 1951 Act, if it is not a subsidiary company of a public company

Besides these special concessions, a private company also enjoys the following further legal exemptions, provided it is not a subsidiary company of a public company:—

12. Under Section 17, compulsory regulations 79-82 (applicable to public companies) of Table A do not apply to private companies.

13. Under Section 54 -A, the legal restrictions imposed on a public company with regard to financial assistance to be given for the purchase of its shares do not apply to a private company.

14. Under Section 79, certain legal provisions with regard to company meetings and voting, which are applicable to public companies, do not apply to a private company.

15. Under Section 83 A, a private company may have less than three directors.

16. Under Section 86-D, the prohibition on public companies in regard to the granting of loans or the guaranteeing of loans granted to directors does not apply to a private company.

17. Under Section 86 -H, the restrictions imposed upon the power of Management of the directors of a public company do not apply to the directors of a private company.

18. Under Section 87-A, the Managing Agents in a private company can be appointed for a period longer than 20 years.

19. Under Section 87-C, the remuneration of the Managing Agents of a private company can be fixed in any manner.

20 Under Section 87-D, the restriction on the granting of loans to Managing Agents does not apply to a private company.

21. Under Section 91-B, the prohibition on voting by interested directors is not applicable to a private company.

22. Under Section 91-D, provisions requiring an agent of a public company (who makes a contract in his own name, but on behalf of the company as an undisclosed principal) to make a memorandum of the contract and file it in the company's office, do not apply to a private company.

23 Under Section 144, a private company is also exempted from having its accounts audited, and its auditors, if any, need not necessarily be Chartered Accountants.

Subject to the above-mentioned privileges, whatever is stated in respect of a public company in the following pages, will also apply to a private company.

PUBLIC COMPANY:—A public company is not defined by the Act, but it means a company which is not a private company; and what is a private company is already defined above. A public company is a company the membership of which is open to the general public under the provisions of its articles. It can offer its shares to the public through prospectus. It also does not impose any restrictions which are necessary in the case of a private company. Any person having a contractual capacity can become a member of a public company. The minimum number of persons required to form such a company is seven, but there is no limitation to the maximum number of members

PRIVATE AND PUBLIC COMPANY DISTINGUISHED

A private company differs from a public company in several important respects on account of the above-mentioned legal exemptions which a private company enjoys over the public company. The salient points of distinction between the two are illuminating from the following chart:—

NO.	BASIS OF DISTINC- TION	PRIVATE COMPANY	PUBLIC COMPANY
1	Minimum number of members.	The minimum number of members in a private company is two.	A public company must have at least seven members.
2	Maximum number of members	The maximum number of members in a private company is fifty, excluding those who are in the employment of the company. But when two or more persons hold shares jointly, they shall be treated as a single member.	The maximum number of members in a public company is limited only by the number of shares issued.
3	Allotment of Shares.	A private company may allot shares immediately after its incorporation.	A public company cannot allot its shares unless it complies with the requirements of Section 101.
4	Commencement of business.	A private company can commence business immediately after its incorporation.	A public company cannot do so unless it complies with the requirements of Section 103.
5	Statutory Meeting.	A private company is not required to hold the statutory meeting and to file the statutory report.	A public company is legally required to do so.
6	Transfer of Shares.	In a private company there is a restriction on the transfer of shares by its Articles.	In a public company the shares are fully transferable.
7	Issue of Prospectus.	A private company cannot issue a prospectus and it is not required to file a statement in lieu of prospectus.	A public company must issue a prospectus, or in the alternative, a statement in lieu of prospectus.

8	Filing of Documents.	It is not necessary to file with the Registrar the following documents:— (a) Consent of directors; (b) List of directors, and (c) Contract of directors, and its Memorandum of Association may be signed only by two persons.	Here consent of at least seven directors must be obtained on the Memorandum of Association. The List of directors along with their consent and contracts, must be filed with the Registrar at the time of incorporation.
9	Retirement of directors.	In a private company directors are not subject to retirement by rotation. There may be less than three directors.	Here two thirds of the directors must retire by rotation. There must be atleast three directors in a public company.
10	Final Accounts.	In a private company the Profit and Loss Account and the Balance Sheet need not be circulated amongst the members. The accounts need not be audited by a Chartered Accountant. But the same must be placed in the Annual General Meeting. Preference shareholders are not entitled to inspect the audited accounts.	Three copies of Profit and Loss Account and the Balance Sheet must be filed with the Registrar; the accounts must be annually audited by a registered auditor; and the same should be sent to all the members before the Annual General Gathering.
11	Managing Agents.	In a private company the appointment of managing agents as well as the fixation of their remuneration are free from all restrictions. The managing agents in a private company can borrow funds from the company and appoint more than one-third of the directors.	Managing Agents can be appointed only for 20 years at a time Their remuneration is fixed in advance as a percentage of the net profit of the company with a certain minimum in addition to office allowance. Loans to managing agents are disallowed.

12	Share Warrants	In a private company share warrants to bearer cannot be issued.	Here share warrants to bearers can be issued, provided the shares or stocks are fully paid.
13	Finance	In a private company financial assistance can be given for the purchase of its own shares, and loans be granted to the directors.	Here no such finance and loans are permissible.

PRIVATE COMPANY AND PARTNERSHIP DISTINGUISHED

A private company also differs from a partnership concern in the following essential points :—

BASIS OF NO. DISTINC-TION		PRIVATE COMPANY	PARTNERSHIP
1	Liability	The liability of the members of a private company is limited to the nominal amount of shares held by them.	In a partnership firm each partner is jointly and severally liable for all the debts of the firm.
2	Maximum number	In a private company the maximum number of members is fixed at fifty.	Here the maximum number is 20 for an ordinary business and ten for banking.
3	Entity	A private company has a legal entity apart from its members with a perpetual succession of members and is not dissolved by the death of a member.	No separate entity in the eyes of law.
4	Creation	A private company is created by registration	A partnership firm may be created either by

5	Mutual relation	under the Indian companies Act. A member of a private company is not its agent and he is not entitled to take active part in its management.	an agreement or by operation of law. In the case of a partnership firm, every partner is an agent of the firm and of his other partners for the purposes of partnership business and he is entitled, in the absence of a contract to the contrary, to take an active part in the management.
6	Transfer of Shares	In a private company shares are transmitted to the heir on death of the member, and the company, as such, continues.	No transfer of interest is possible unless other partners agree. Death of a partner results in the dissolution of the firm.
7	Debentures etc.	Debentures and Redeemable Preference shares are issued for raising fresh capital.	In a partnership concern loans are arranged only on personal credit or against pledge of personal property.
8	Registration	Registration of a private company with the Registrar of Joint Stock Companies is compulsory, otherwise the association shall be illegal.	Registration of partnership concerns is optional.
9	Interest	A member's interest in a company may be divided into several parts and be bequeathed to persons who cannot assume the role of true partners.	The interest in the partnership is absolutely one and inalienable. Successor can not be admitted into the firm, nor can they acquire any kind of control in its management.

10	Regis- tration of powers	The general powers of a private company are governed by its memorandum of Association which can be altered only with the consent of the court and that also to a limited extent.	The general powers of a private concern are regulated by agreement which may be freely altered if all the partners so desire.
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LIMITED LIABILITY COMPANY AND PARTNERSHIP

The main points of contrast between a limited liability company and a partnership are given below :—

NO.	BASIS OF DISTINC- TION	COMPANY	PARTNERSHIP
1	Separate Entity	A company has a separate entity from that of its shareholders. It is governed by the Indian Companies Act, which it cannot over ride. Its powers are fixed by the Memorandum of Association.	Partnership has no individuality of its own, apart from the individuality of its members.
2	Number of mem- bers	In a public company the minimum number of members is fixed at 7. The maximum number in a public company is limited by the number of shares the company is authorised to issue; and in case of a private company the maximum is fixed at 50 (excluding the present employees).	In a partnership concern, the maximum number may not exceed 20, and if the business carried on is banking, they must not exceed 10. If the number is in excess, the partnership is illegal and cannot enforce its claims against outsiders.

3	Incorporation	A joint stock company has to be registered with the Registrar of joint Stock Companies, and unless registration or incorporation is complete, the company does not come into existence.	Partnership firm may or may not be registered. Even if the firm is unregistered, the agreement between the partners inter se, or between the partners and third parties will be perfectly valid, though not enforceable.
4	Liability	The liability of a shareholder is limited to the nominal amount of the shares held by him.	In a partnership firm the liability of each partner is co-extensive with the whole of his property, every partner is jointly and severally liable for all the debts of the firm incurred while he is a partner.
5	Management	A shareholder has no power to bind the company or to bind the other shareholders, nor can he take any active part in the management of the affairs of the company. The rights of management in a company are delegated to directors, who alone can bind the company. The shareholders also cannot inspect the books except as may be allowed by the Articles.	In partnership each individual member can normally take part in the management of the business and can also bind the firm and his co-partners so long as he acts within the ordinary scope of the business. Each partner has full access to the books and accounts of the firm. There is no divorce between ownership and management.
6	Transferability	A shareholder in a public company can transfer his shares according	A partner cannot ; except by agreement with his co-partners

		to his sweet will. In a private company, however, there is restriction over the transferability of shares. Thus the members of a company may change, yet the company retains the same entity and is not affected by such changes.	substitute another partner for himself.
7	Memo- randum	A company is bound by its memorandum and articles of association. These documents can be changed only to a limited extent as provided by law.	The partners can make any agreement as they choose, and can alter the terms of partnership as and when they please.
8	Audit and Accounts	A company must keep proper books of account. Audit of a limited concern is compulsory. The failure to keep the prescribed books of account renders the company liable to serious penalties.	There is no statutory provision requiring a partnership to do so.
9	Contract	A shareholder of a company can contract with the company.	A partner cannot contract with his firm.
10	Dissolution	A company comes to an end by an order of the court, or by the resolution of members for voluntary winding up, or by the decision of its creditors who cannot be paid in full.	Partnership can be dissolved by mutual agreement at any time. It also comes to a fullstop by the death or retirement of a partner (unless there is a contract to the contrary).

11	Distri- bution of profits	The profits of a com- pany are distributed by means of dividends passed by a resolution in a general meeting. If the profits are good, the directors may declare interim dividends.	In partnership profits may be withdrawn as and when ascertained or periodical drawings in advance may be resorted to by mutual agreement. The capital contributions of the different partners may thus be increased or decreased.
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HOLDING AND SUBSIDIARY COMPANIES :—The holding company and subsidiary company are relative terms, and are used only in connection with the relation of two companies. One of which holds a majority of the voting capital in the other company or possesses the power to nominate the majority of the directors of the other company. The term holding company is not defined by Indian Company Law but its definition can be ascertained from the legal definition of a subsidiary company as given in section 2 (2). According to this section where a company holds shares in another company directly or through a nominee and—

(i) The amount of shares held is more than 50 percent of the issued share capital of the other company, or

(ii) the share holding is such as to entitle the company to more than 50 P. c. of the voting power in the other company, or

(iii) the company enjoys the right to nominate majority of directors of that other company.

Then this latter company is known as a “subsidiary company,” and a “holding company” is one which has such an interest in one or more of the subsidiary companies. It shall not be out of place to mention here that the term ‘subsidiary company’ also includes sub-subsidiaries of its own. A subsidiary company may be public or private, and it may be a holding company of another subsidiary.

ILLUSTRATION :—If the assets of A company consist in whole or in part of shares in company B, so that (i) the amount of shares held by the former company is more than 50 p. c. of the issued share capital of B company, or (ii) the former company

monopolises more than 50 p. c of the voting capital, or (iii) the former company enjoys the power to appoint directly the majority of the directors of B company ; then A company is the Holding company and B company is the Subsidiary Company.

It is also possible that a subsidiary company may be a subsidiary company of more than one holding company simultaneously. The following illustration is illuminating in this connection :--Thus, if S company has a share capital consisting of 1,200 preference shares of Rs. 100/- each, carrying one vote per share ; 10,000 ordinary shares of Rs. 10/- each, carrying one vote per share, and 1,000 deferred shares of Re 1/- each, carrying one vote per share and also possessing the right to appoint 60 P. c. of the directors ; and each class of shares is held by a different company, then the S company will be deemed as a subsidiary company of the three holding companies, because (i) the first holding company monopolises more than 50 P. c. of the issued share capital ; (ii) the second company possesses more than 50 P. c. of the voting power and (iii) the third holding company enjoys the right to appoint the majority of the directors of S company.

It should also be noted in this connection that an INVESTMENT COMPANY, i.e. a company whose principal business is the acquisition and holding of shares, stock, debentures or other securities, is not a holding company merely because part of its assets consists in 50 P. c. or more of the shares of another company.

ASSOCIATIONS NOT FOR PROFIT :—Under section 26, certain association (which are not for profit) may be registered as a limited company—but without the word ‘Limited’—provided that they obtain a license from the central government. The Central Government may grant license on such terms and conditions as it may think fit, and those conditions and regulations shall be binding on the association, and shall be inserted in its memorandum and articles. Before granting the license, the Central Government must be satisfied that the association is to be formed for promoting commerce, art, science, religion, charity, or any other useful object and applies or intends to apply its profits in promoting its objects, and to prohibit the payment of any dividend to its members. Such an association shall, on registration, enjoy all the privileges of limited companies, except those of using the word “Limited” as any

part of its name, publishing its name and sending of lists of members to the Registrar.

Under sub section 4 of section 26, the license granted to an association not for profit may at any time be revoked by the Central Government, and upon revocation the registrar shall enter the word "Limited" at the end of the name of the association upon the register, and the association shall cease to enjoy the exemptions and privileges granted by section 26. The memorandum and articles of such an association are exempt from stamp duty.

CHAPTER II.

CONSTITUTION AND INCORPORATION

PROHIBITION OF LARGE PARTNERSHIP

Under section 4 of the Indian Companies Act, no company, association or partnership consisting of more than 20 persons (and not more than 10 in the case of a banking business) can be formed for the purpose of carrying on any business with the object of making profit unless it is registered as a company or is formed in pursuance of an Act of Parliament or some other Indian Law or of Royal Charter of Letters Patent. As already remarked in the previous chapter, an association of more than 20 persons, which exists not for gain but for some other purpose, such as the promotion of commerce, art, science, charity etc., may be formed under a license from the Central Government and does not require registration. The main object of this section is to prevent the mischief arising from large trading businesses being carried on by large fluctuating bodies, in order that persons dealing with them do not know with whom they are contracting and may, therefore, be put to unnecessary trouble and expenses.

This section 4 does not apply to a joint Hindu family carrying on joint family trade or business, and where two or more such joint

families form a partnership, in computing the number of persons, minor members of such families shall not be included. It should also be noted that where two or more joint Hindu families combine with one another for carrying on a business, each joint family shall not be deemed as one person, but as many persons as there are adult members in each of the joint families. A registered company would, of course, be considered as one person.

Any association formed contrary to the provisions of section 4 shall be an illegal body, and its consequences are as below .—

(1) Every member of a company, association or partnership carrying on business in contravention to the provisions of section 4 shall be personally liable for all liabilities incurred in such business. In other words it means that a suit would be against every member and not against the illegal association for enforcing all liabilities incurred in the business of such association, irrespective of whether the plaintiff had and had not notice of the illegality of the association.

(2) Such an illegal association loses the right to sue, even if it is subsequently registered.

(3) Every member of such an illegal association shall be punishable with fine not exceeding Rs 1,000 .-

FORMATION OF A COMPANY

A joint stock company may be formed in any one of the following three ways —

- (1) By Royal Charter, known as chartered companies ;
- (2) By a Special Act of Legislature, known as Statutory Companies, or ,
- (3) By Incorporation under the Indian Companies Act, known as Incorporated Companies.

In this book we are concerned with the formation of incorporated companies only.

MODE OF FORMING INCORPORATED COMPANY :

In the formation of a company, a certain amount of preliminary work is necessary before a company can come into existence, and the person who does this work is known as the **PROMOTER**. The term, 'Promoter' is not a term of law, but is used in Common parlance to denote any individual, firm, syndicate, association or

company, which takes all necessary steps to form a company and to get it going. The usual functions of a promoter in connection with the flotation of a company may be enumerated as follows :—

(1) It is the promoter who chalks out the idea of forming a company, explores its possibilities and does the entire preliminary research.

(2) He drafts the original documents like the Memorandum and Articles of Association, Prospectus etc. and procures persons who may sign the Memorandum of Association.

(3) The promoters also select the first directors of the company.

(4) They (promoters) settle the name of the company, the amount of capital and its structure or form and also arrange for underwriting if necessary.

(5) They select the bankers, auditors, brokers, legal advisers etc.

(6) They attend to the registration of the company.

(7) They arrange for the completion of contracts with underwriters, managing agents etc.

(8) They arrange for the filing, issue and advertisement of the prospectus,

(9) They purchase the property required for the carrying on of the proposed business and do all other things to float the company.

(10) Last, but not the least, the promoters also pay the preliminary expenses.

Thus, in short, the promoters play the supreme role in the formation of a company. For all this work they receive some remuneration, and so long as the remuneration is received in good faith and with due disclosure, it is valid in law. The remuneration of the promoters may be in cash or partly in cash and partly in shares and debentures of the company. It shall not be out of place to mention in this connection that in India, the promoters do not take any remuneration for their services, but in lieu of it they become the managing agents of the companies they promote. They prefer to become managing agents specially because as managing agents they are able to earn a lot for themselves.

The promoter is not a trustee or agent of the company, but he stands in a fiduciary relation towards it and is liable, like other directors, to refund secret profits, if any, made without the company's knowledge and consent. In the case of fraud, the promoter shall be liable for damages sustained by the company ; and on his death, his estate will remain liable if it has benefitted from the deceit or breach of trust, but not otherwise.

THE PRELIMINARY CONTRACT . A preliminary contract means a contract made between the promoter on the one hand and the vendor or leasor on the other, when a company is formed for the purpose of buying an existing business or property. A preliminary contract entered into prior to incorporation is not binding on the company nor can it be ratified by the company after incorporation, because according to contract Act, a person cannot act as an agent for another who is not yet in existence. The company also cannot sue the vendor, if he fails to carry out the contract. The persons purporting to enter into contract on behalf of the company remain personally liable on the preliminary contract. Even if it is afterwards ratified by the company. On account of these difficulties, what is actually done is that as soon as a company is incorporated, it enters into a new contract with the promoter to carry out the terms of the preliminary contract, and this is known as the 'ratification' or adoption of the preliminary contract.

LEGAL FORMALITIES IN THE FORMATION OF A COMPANY :

A limited liability company is formed by filing the following documents with the Registrar of Joint Stock Companies of the province in which the registered office of the company is to be situated :—

(1) Memorandum of Association and Articles of Association signed by at least seven persons (section 22). Where the company adopts Table A completely, it need not file any special articles, but this fact must be endorsed on the Memorandum of Association.

(2) A list of persons who have agreed to become the directors of the company. (Section 84).

(2) Under the same section 84, where the first directors of the company are appointed by the articles, each such director must

sign and file with the Registrar—(i) a written consent to act as director and (ii) either sign the memorandum for a number of shares not less than his qualification shares, if any, or sign and file with the Registrar and pay for his qualification shares or make out and file with the Registrar an affidavit to the effect that a number of shares not less than his qualification shares are registered in his name

(4) A statutory declaration by an advocate or an officer of the company that the requirements of law for registration have been complied with (Section 24).

(5) Notice of the situation of the registered office of the company (Section 72).

(6) Prospectus or a statement in lieu of Prospectus signed by every person who is named there in as a Director (Sections 92 and 98). These documents may be filed either at the time of incorporation or shortly afterwards.

After the filing of the aforesaid documents the next step should be to pay the requisite amount of duty and the prescribed amount of filing fees to the Registrar. The payment can be made by depositing the amounts into a Government Treasury. The amount of duty varies according to capital as shown below :—

(i) Where the capital does not exceed Rs. 20,000/- .. Rs. 40-0-0

(ii) Where the capital exceeds Rs. 20,000/- for every

Rs. 10,000/- or part thereof upto Rs. 50,000/- .. Rs. 20-0-0

(iii) For every Rs. 10,000 - or part thereof beyond

Rs. 50,000 - and upto Rs. 10,00,000/- Rs. 5-0-0

(iv) For every Rs. 10,000/- or part thereof beyond

Rs. 10,00,000/- Re. 1-0-0

The maximum duty payable on any capital is Rs. 10,000/-. In the case of an increase in the share capital, the additional duty to be paid will be the difference between the duty payable on the increased capital and the duty that has actually been paid. The filing fee for each document is Rs. 3/- only.

When these legal formalities are observed to the satisfaction of the Registrar, he will enter the name of the company in the register, and will then issue a **CERTIFICATE OF INCORPORATION**, which gives the company a legal existence from the date

given on it. This certificate is a conclusive evidence that the requirements of law have been complied with and that the company has come into legal existence, with rights and liabilities of a natural person, competent to enter into contracts.

A public company cannot commence business without obtaining a **CERTIFICATE TO COMMENCE BUSINESS**, which is granted by the Registrar only when, along with other formalities of law, "Minimum Subscription" has also been allotted (Section 103).

NOTE :—

[A private company can be formed by filing with the Registrar only (i) the Memorandum and Articles of Association, (ii) Statutory declaration and (iii) notice of the registered office, and by paying the same amount of capital duty and filing fees as in the case of public companies]

Now we shall deal in detail with the important documents required to be filed with the Registrar on the registration of a company.

MEMORANDUM OF ASSOCIATION

DEFINITION OF MEMORANDUM OF ASSOCIATION

A Memorandum of Association is, in fact, a Charter or constitution of the company and contains the fundamental conditions on which incorporation is granted. It is the most important document of the company as it defines its objects and governs its powers. The main purpose of the memorandum is to enable the shareholders, creditors and all those who deal with the company to know what is the scope of its activities.

CONTENTS OF A MEMORANDUM OF ASSOCIATION

Contents of the memorandum differ according to whether the company is limited by shares or by guarantee or is an unlimited company. However, the following are the provisions of law in each case as required by sections 6, 7 and 8.

The memorandum of association must state :—

1. THE NAME CLAUSE :—A company is free to adopt any name it likes, but it is always better to ascertain from the Registrar beforehand whether the name chosen is available for registration or not. It is advisable to choose a name which gives some indication of the company's business. The name may include

personal names or it may be of an impersonal character. The following rules should be remembered in this connection :—

(a) The name of the company may include the word 'company', or exclude it, but in the case of a company limited by shares or by guarantee, the word 'Limited' must be used as the last word in the name (section 12).

(b) The name of the company must not be identical with that of another existing company so as to create confusion and lead people to believe that the company is carrying on the business of an already existing company.

(c) Section 11 further prohibits the use of the following words without prior consent of the central Government—Crown, Emperor, Empire, King, Queen, Royal, State, Empress, Federal, Imperial, Reserve Bank, Bank of Bengal, Bombay or Madras or any other name which suggests the patronage of His Majesty or any member of the Royal family.

(d) The name should not also contain the word 'municipal' or 'chartered' or any other word which suggests connection with any municipality or other local authority or with any society or body incorporated by Royal charter.

(e) The name should not contain the word 'co-operative' without prior approval of the state-government, or unless it is registered under the co-operative Societies Act.

(f) Under section 73, the name of the company must (i) be painted or affixed on the outside of every office and the place where the business of the company is transacted; (ii) be engraved on its seal, and (iii) be mentioned in all notices, advertisements and other business documents.

2. THE SITUATION CLAUSE :—The clause provides for stating the name of the State in which the registered office of the company is to be maintained. The place of the registered office determines the domicile and the nationality of the company. It is the place where the records of the company are to be kept. The registered office must be arranged from the day on which the company commences its business or from the 28th day after its incorporation, whichever is earlier.

3. THE OBJECTS CLAUSE :—This clause is of supreme importance, as upon this depends the entire scope of a company's

operations. The objects of the company should be lawful and must be fully and clearly stated. Anything done beyond the objects stated in the Memorandum shall be ultra vires and therefore invalid.

4. **THE LIABILITY CLAUSE:**—In the case of a company limited by shares or by guarantee, a declaration must be made in the memorandum that the liability of the shareholders is limited to amounts unpaid on their shares. Thus, if P has subscribed for Rs. 50/- share and has paid only Rs. 25/- on it, he can be required to pay another Rs. 25/- in the event of its dissolution and the assets being insufficient to pay the creditors. A shareholder who has paid up the full value of the share, cannot be made to pay anymore. Also, where such a shareholder sells his share to a third person, even for a nominal amount of Rs. 5/-, such third person cannot be made to pay anything. But there is one exception to this general principle, viz, that if a company continues to carry on business for more than six months after the membership has fallen below seven in the case of a public company and below two, in the case of a private company, all members aware of the fact are fully and severally liable for all debts contracted after the six months.

5. **THE CAPITAL CLAUSE:**—In the case of a company having a share capital, the memorandum must contain a statement as to the amount of capital with which the company proposes to be registered, divided into shares of a certain fixed amount.

In the case of a company limited by guarantee, the memorandum must state that each member undertakes to contribute to the assets of the company in the event of its being wound up while he is a member, or within one year after he ceases to be a member, for payment of the debts and liabilities of the company contracted before he ceases to be a member, and of the expenses of winding up, and for adjustment of the rights of the contributories among themselves, such amount as may be required, not exceeding a specified sum.

Under Section 9, the memorandum must be :—

- (a) Printed;
- (b) Divided into paragraphs numbered consecutively, and;
- (c) Signed by each subscriber (at least seven, who shall add their address and description) in the presence of at least one witness (two in the case of a private company), and each subscriber

must take atleast one share and write opposite his name the number of shares taken. It should be noted in this connection that only a person *sui juris* or competent to contract can subscribe to the memorandum. A minor or a partnership firm cannot, although individual partners can, subscribe to it. An insolvent can subscribe.

ALTERATION OF MEMORANDUM :

According to Section 10, the conditions contained in a memorandum cannot be altered after registration except in the cases and in the mode and to the extent for which express provision is made in the Act Section 11—I6 and proviso to Sec. 10 permits the alteration of the memorandum in the following cases, provided that the legal procedure is strictly followed :—

1 CHANGE RELATING TO APPOINTMENT OF MANAGER OR MANAGING AGENT:—Any provision relating to the appointment of a manager or managing agent and such other matters which are subsidiary to the main object of the company, can be altered at any time merely by an ordinary resolution of the company, because such matters are not to be treated as 'conditions' in the memorandum.

2. CHANGE OF NAME CLAUSE:—The name of the company can be altered in two ways:—

(i) It can be changed simply with the sanction of the Registrar if a company has inadvertently adopted a name identical with that of another existing company.

(ii) In any other case, the name of the company can be changed by passing a special resolution and with the approval of the central government. Such a change should be communicated to the Registrar who will issue a fresh Certificate of Incorporation. The change of the name clause does not affect the existing rights and obligations of the company, nor does it affect any legal proceedings commenced under the old name.

3. ALTERATION OF REGISTERED AND OBJECTS CLAUSE:—A company may, under the following provisions of Section 12, change its registered office from one state to another or may alter its object clause by a special resolution and with the sanction of the court on petition after due notice to all concerned, if such change will enable it :—

(a) To carry on its business more economically or more efficiently; or

(b) To attain its main purpose by new or improved means, or.

(c) To enlarge or change the local area of its operations; or.

(d) To carry on some business which under existing circumstances may conveniently or advantageously be combined with the business of the company; or.

(e) To restrict or abandon any of the objects specified in the memorandum, or.

(f) To sale or dispose of the whole or any part of the undertaking of the company; or.

(g) To amalgamate with any other company or body of persons.

The above alteration will not be effective until it is confirmed by the court. Before confirming the alteration, the court must be satisfied :—

(a) That sufficient notice has been given to every debenture-holder and any persons or class of persons whose interests will, in the opinion of the court, be affected, and.

(b) That with regard to every objecting creditor, either his consent to the alteration has been obtained or his debt or claim has been discharged, determined or secured to the satisfaction of the court. The court will also have due regard for the interest of the members.

A certified copy of the order of the court together with a printed copy of the altered memorandum must also be filed within three months of the date of the order with the Registrar, who will register them and issue a fresh Certificate of Incorporation which shall be a conclusive evidence that everything has been done properly. Where the alteration involves the transfer of the registered office from one state to another, these documents must be sent to the Registrar of each state and Certificates obtained. All the papers of the company will then be transferred by the Registrar of the old state to the registrar of the new state

4. ALTERATION OF LIMITATION OF LIABILITY
CLAUSE:—The limitation of liability of the members cannot be disturbed in toto. However under Section 71, a limited company may alter its memorandum by special resolution so as to render

unlimited the liability of its directors, provided that the company is authorised by its articles to do so.

5. **ALTERATION OF CAPITAL CLAUSE:**—The contents of a memorandum relating to share capital may be altered as below :

(i) Under Section 50, a company limited by share, if so authorised by its articles, may :—

(a) Increase its share capital by the issue of new shares of such amount as it thinks expedient.

(b) Consolidate and divide all or any of its share capital into shares of larger amount than its existing shares.

(c) Convert its fully paid up shares into stock and reconvert the stock into paid up shares.

(d) Sub-divide its shares into shares of smaller amounts; or.

(e) Cancel its unissued shares.

Such an alteration must be exercised by the company in general meeting. The nature of resolution to be passed will be indicated by the articles of the company; otherwise an ordinary resolution would do. Under Section 105 C, in the case of increase in capital by the issue of more share, the additional shares must be offered to the existing members in proportion to the shares held by them, irrespective of class, but in case the offer is not accepted within the stated time, the directors may dispose of them in the possible manner. Notice of any alteration under Section 50 must be filed with the Registrar within 15 days, and if default is made in this respect, both the company and every officer party there to shall be liable to a fine upto Rs. 50/- a day so long as the default continues. In the case of increase of share capital the requisite amount of capital duty should also be paid, and all the copies of memorandum issued after the alteration must show the new capital.

REDUCTION OF SHARE CAPITAL : Under section 55, a company, if authorised by its articles, may reduce its share capital by special resolution confirmed by the court in any of the following ways :—

(a) by reducing or extinguishing the liability of members for uncalled capital ;

(b) by writing off lost capital ;

(c) by paying off capital which is in excess of the requirements of the company .

(d) in any other way which may be approved by the court.

Where however, reduction of share capital involves diminution of liability for unpaid capital or return to any shareholder of any paid up capital, all creditors of the company are entitled to object to the reduction (section 58 (1)). Under such a circumstance, the court shall prepare a list of creditors and hear their objections ; and prior to the sanction of the scheme for reduction, the consent of the creditors must be obtained or some satisfactory arrangement be made in order to protect their interests. The court may order the words "and Reduced" to be added to the name of the company for such period as may be directed. The court may also direct the company to publish the reasons for reduction for general information (section 60). A copy of the resolution duly confirmed by the court should also be filed with the Registrar who will, then, issue a fresh certificate which will be conclusive evidence that everything has been done in order (Sec. 61).

No sanction of Court is required in the following cases for the reduction of capital :—

- (a) Upon the forfeiture of shares ;
 - (b) Where the shares held by a company have been disclaimed under sec. 230-A by its liquidator, and the company affected by the disclaimer removes the name of the holder from its register ;
 - (c) Upon the cancellation of unissued shares under sec, 50 ;
- or
- (d) On the redemption of redeemable preference shares under section 105-A.

When different classes of shares are issued by a company, it would be equitable to apportion the incidence of loss caused by the reduction of capital between the different classes of shareholders according to their respective rights. Where the lost capital is written off all the different classes of shares, it is technically known as, what we call, an "all-round reduction "

VARIATION OF THE SHAREHOLDERS' RIGHTS :

When the rights attached to the different classes of shares are fixed by the memorandum of association, these can be altered in accordance with the provision made in that behalf by the Memo-

random and Articles of Association. The usual provision is that the rights attached to the different classes of shares can be altered subject to the consent any specified proportion of the whole of the issued shares of that class or with the sanction of the resolution passed at a separate class meeting of the holders of those shares. Section 66-A provides that, if the rights are so varied, the dissenting minority holding not less, in the aggregate, 10 p. c. of the issued shares of that class may apply to the court for the cancellation of such variation within 14 days from the date on which the consent was given or the resolution was passed. The court will, then, hear the applicants; and may, if it is satisfied that the variation would unfairly prejudice the shareholders of the class represented by the application, disallow the variation, and shall, if not so satisfied, confirm the variation. Such decision of the court shall be final (Sec. 66-A, sub Sections 1—4). The company is also required to forward within a fortnight after the service to the company of order made in such application, a copy of the order to the Registrar and, in case of default) the company and every officer of the company responsible for default shall be liable to a fine not exceeding Rs. 50/-.

When the rights attached to the different classes of shares are fixed by the Memorandum; but the memorandum does not empower to alter them the rights can be changed in accordance with the provisions of Section 153. Under this Section it is possible to put through any scheme of arrangement between the company and its members. Accordingly, an application has to be made to the court for directions as to holding the class meetings of shareholders affected by the proposal; the scheme in order to be effective must be passed by the prescribed statutory majority and then approved by the court.

ARTICLES OF ASSOCIATION

MEANING OF ARTICLES :

The Articles of Association are the rules and bye-laws for carrying into effect the objects defined in its memorandum and for the internal management of the company. Under Sec. 2 (1) of the Act the articles mean the articles of association of a company as originally framed and as altered by special resolution. They define

the powers of the directors and officers, and the rights of shareholders as regards return of capital, dividend, voting etc.

REGISTRATION OF ARTICLES WHEN NECESSARY AND VICE VERSA

In case of a company limited by shares registered after the commencement of the Indian companies Act 1913, it is not absolutely necessary to register any articles, because if such articles are not registered, the regulations in TABLE A will automatically apply. But it is proper and usual to register a set of articles for the management of the company, and in so far as the articles do not exclude or modify the regulations in Table A, the latter will apply (Section 18). Table A is a model set of 116 articles contained in the First Schedule of the Act.

Private companies, unlimited companies and companies limited by guarantee must file their own articles, as they cannot adopt Table A completely. The articles of a private company must include provisions in accordance with Section 2 (13) and must also restrict certain clauses of Table A, which do not apply to private companies. In the case of a company limited by guarantee or an unlimited company, the articles must state the amount of share capital, and if it has no share capital, the number of members with which it proposes to be registered (Section 17). Under Section 17 (2), regulations 56, 66, 71, 95, 97, 135, 107 and 112—116 of Table A compulsorily apply to all companies, and its regulations 78—82 apply to all public companies. Thus, the articles must be registered in the case of a company limited by guarantee or an unlimited company.

While drafting the articles of a company and getting them registered, the following important points must be remembered :

1. The articles must not contain anything which is against or repugnant to the provisions of the Indian companies Act, and must be rejected if they are inconsistent therewith or the general law.

2. Under Section 17 (2), articles of every company must contain the following provisions of Table A :—

- (i) Regulation 56 relating to the mode of decision of a resolution put to vote at a general meeting.

(ii) Regulation 66 relating to the deposit of instrument appointing a proxy and power of attorney relating thereto 72 hours prior to the holding of the meeting.

(iii) Regulation 71 relating to the management of the business of the company by the directors.

(iv) to (viii) Regulations 78 to 82 relating to the rotation, retirement of directors, their eligibility for re-election and filling up of vacancies caused by rotation and retirements. (These regulations shall not be deemed to be included in the articles of any private company except one which is the subsidiary of a public company.)

(ix) Regulation 95 relating to declaration of dividend not exceeding the amount recommended by the directors.

(x) Regulation 97 relating to the payment of dividend only out of the profits for the year or any other undistributed profits.

(xi) Regulation 105 relating to the provisions regulating the inspection of the account books of the company by its members.

(xii) Regulation 107 relating to the requirements of the profit and loss accounts.

(xiii) to (xvii) Regulations 212 to 216 relating to notice to the members of their legal representatives and mode of service thereof.

3. The Articles of association are subordinate to the Memorandum, and hence they should not be inconsistent with any of its provisions.

4. The articles must be printed, divided into paragraphs numbered consecutively and should also be signed by each subscriber of the memorandum, who shall add his address and description in the presence of at least one witness who must attest the signature (Section 19).

5. In the case of an unlimited company or a company limited by guarantee, if the company has a share capital, the articles must state the amount of share capital and the number of members with which it proposes to be registered.

The following are the salient points of distinction between a memorandum and articles of association :—

NO.	BASIS OF DIFFE- RENCE	MEMORANDUM	ARTICLES OF ASSOCIATION
1	Nature.	(a) It is a contract between the company and the outside world dealing with it. (b) Memorandum contains the fundamental conditions on which incorporation is granted and those terms are unalterable. (c) It defines the objects and powers of the company.	(a) Articles govern the relations of the shareholders and the officers of the company inter Section. (b) Articles can be altered by the shareholders according to their sweet will by means of a special resolution. (c) It contains the byelaws and regulations for carrying into effect the objects and powers given in the memorandum.
2	Scope.	It is subordinate only to the Indian companies Act and cannot do any thing inconsistent with the provisions of the Act	The articles are limited not only by the Act, but they are also subordinate to the memorandum and cannot exceed the powers contained therein.
3	Bearing on outsiders.	A customer of the company is expected to know the contents of its Memorandum, e. g., if he enters into a contract which the Memorandum does not entitle the company to undertake, he cannot enforce the same at law.	A customer of the company is expected to know its articles but if there is a breach, he is not affected thereby provided he had no notice of such breach, e. g., if he pays money in advance of the calls subject to a rate of interest higher than that allowed by the articles, he can enforce the higher interest-rate at law.

EFFECT OF ARTICLES :

The effect of the articles is to create a contract between the company and its members. Under Sec. 21, the articles bind the company and the members (as well as their heir and legal representatives to the same extent as if each member had signed them and they contain a covenant by him to observe all the provisions thereof. As a consequence if a member fails to observe them, e. g., does not pay up his calls he can be sued against by the company; similarly, if a member's shares have been forfeited by the company against the provisions of its articles, he can sue the company for the same. This, however, does not apply to outsiders who are no party to the articles.

As between the members inter se, each member is bound by the articles to the other members, but it does not mean that the articles or the memorandum create an express contract between the members of the company. A member, therefore, has no right to bring a suit in his own name against any other member or members; it is only the company that can file a suit against the offender. There is, however, one exception to this rule, that the shareholders may sue in their own name, if the persons against whom relief is sought control the majority and they will not allow a suit to be filed in the name of the company. The acts complained of must be *ultra vires** and not mere informalities or irregularities.

"The members of a company are not bound to outsiders even if their names have been mentioned in the Memo. or Articles in connection with the business of the company. But, of course, the articles may embody a contract with an outsider who can sue the

***ULTRA VIRES :—**The doctrine of *Ultra vires* applies to all companies. According to it if the following acts of a company shall be *ultra vires*, i. e., beyond the power of a company :—

(i) Those that are *ultra vires* the memorandum, e. g., acts beyond the object of the memorandum shall be null and void.

(ii) Those that are *ultra vires* the articles, but *intra vires* the memorandum, e. g., paying interest on calls in advance at a rate higher than that allowed by the articles. Such acts are void, but may, however be ratified subsequently.

(iii) Those that are *ultra vires* the directors but *intra vires* the company, e. g., payment of a gratuity to an employee of the company by the directors who are not authorised to do so. Such act shall be void; but they can also

company. Thus in Eley's case, a company named in its memorandum and articles one Eley as its solicitor and legal adviser, but later on changed its mind. Eley was not allowed any damages, for the articles did not constitute any contract between him and the company. But in the New British Iron. Co., where the articles provided for certain fixed remuneration to be paid to its directors, it was held that though the articles did not constitute a contract between the company and the directors, the directors accepted the office on the footing of the articles and, therefore, the terms of the articles became part of the contract with the company which the directors could enforce. The persons contracting with the company are presumed to have knowledge of the articles, but they are entitled to assume that the provisions of the articles have been observed. This limitation is called the Doctrine of "INDOOR MANAGEMENT" or the RULE IN ROYAL BRITISH V. TURQUAND. The rule does not, however, apply to cases of forgery, or to void transactions, or entitle a contracting party to ignore suspicious circumstances, nor bind the company or officer of the company and such other persons who should know whether the regulations in the articles have been observed*.".

ALTERATION OF ARTICLES :

Companies are absolute masters of their internal regulations, and hence they can alter those regulations from time to time according to requirements, but subject, however, to the conditions contained in the Memorandum of Association. The Memorandum is, as it were, the area beyond which the action of the company cannot go, but inside that area they may make such regulations for their own government as they think fit. Therefore, under Section 20, a company may by a special resolution alter its articles and any alteration so made will be as valid as if originally contained in the articles. The alteration of articles is, however, subject to following restrictions :—

STATUTORY RESTRICTIONS :

(a) Articles can be altered only by special resolution and not by an ordinary or extra-ordinary resolution.

(b) Alteration in the articles cannot supercede the provisions of the Memorandum.

(c) The alteration must not be inconsistent with the provisions of the Act.

(d) No alteration in the articles can be made if the effect thereof is to cast upon a member any liability to purchase more shares than the number of shares already held by him, or in any way to increase his liability as at that date to contribute to the share capital of, or otherwise, to pay money to the company.

RESTRICTIONS IMPOSED BY JUDICIAL DECISIONS :

(a) The articles must be altered in good faith and not so as to give an unfair advantage to a majority of the shareholders and the majority will not be permitted by the court to commit a fraud on the minority.

(b) Alteration should not constitute a breach of contract with an outsider

The Court has, however, no jurisdiction to rectify the articles even on the ground of a mistake. It should also be noted in this connection that notice of meeting on the member effected by the alteration is essential. Accordingly, where a company altered its articles by an addition thereto to provide for the necessary means to force an expelled member to sell his share to any person at a price to be fixed by the articles, but the notice was withheld from such member, it was held that the alteration in question was not binding on the member aforesaid.

PROSPECTUS

(Sections 92—100)

MEANING OF PROSPECTUS :

A prospectus is a document by which an invitation is made to the public to subscribe for or purchase the shares or debentures of a company. As rightly remarked by Messrs Sarcar and Sen in their popular commentary on the Indian Companies Act at page 26. It is difficult to give any rigid or exact definition and the question as to whether a particular document is a prospectus or not would have to be decided on consideration of various factors such as numbers circulated or printed, number of persons to whom it is sent, the circumstances in which such persons receive it and the character of the contents of the documents. If it amounts to an invitation it would be a prospectus although it may have been issued to a defined

class of public.” However, section 2 (14) of the Act defines it as follows :—

Prospectus means any prospectus, notice, circular, advertisement or other invitation offering to the public for subscription or purchase any share or debenture of a company, but shall not include any trade advertisement which shows on the face of it that a formal prospectus has been prepared and filed. The gist of the definition is the offer to the PUBLIC. The word “public” is not defined in the Act while offers made to a limited class of persons, e.g., the distribution of 4,000 copies of prospectus among shareholders in a group of companies have been held to be offers to the public; the friends of the directors and existing members have been held not to be within the category of “public.” In short, a prospectus is an invitation to the members of the public to purchase shares or debentures of the company; and remains a prospectus even when it is issued to a defined class of the public, and marked “Private and Confidential”, or “for private circulation”, although it will not be so when delivered with such words to individuals who—may pass it on among friends and relations. The most important element of a prospectus is invitation to public. The main objects of issuing a prospectus are—(i) to preserve an authentic record of the terms on which the offer is made to the public for the purchase of shares or debentures, and (ii) to secure that the directors accept the responsibility for the statements contained in the prospectus.

Legally a prospectus can be issued even prior to the formation of a company, and a company may issue a prospectus at any stage in its existence, and not merely at its commencement.

FILING OF PROSPECTUS :—

Under Section 92, every prospectus must be dated and a copy thereof signed by every director or proposed director must be filed with the Registrar on or before the date of its publication. Moreover, prospectus should state on the face of it that a copy has been filed with the Registrar, and if a prospectus is issued without a copy thereof being so filed, the company and every person who is knowingly a party to such issue shall be liable to a fine not exceeding Rs. 50/- per day from the date of the issue until the date when the copy is filed.

A prospectus may be circulated by post or otherwise, or it may be advertised in the press. According to Sec. 22 (2), every

form of application for shares or debentures sent out must be accompanied by a copy of the prospectus.

Contents Of Prospectus :—

The preparation of a prospectus involves considerable skill and responsibility. It is the very foundation of a company's edifice, and it is on the basis of the statements contained in a prospectus that the public accepts the offer for shares or debentures. The prospectus should therefore be as attractive as possible and at the same time it should also not contain untrue statements or even vague statements of vital facts nor should it conceal any material fact or circumstance. It should tell the truth, the whole truth and nothing but the truth. It means that while everything must be stated in a prospectus with strict and scrupulous accuracy, it should not omit any such fact the existence of which might in any degree affect the nature, or extent or quality of the privileges and advantages which it holds out as inducement to take shares. It should comply with the general law and the provisions of the Indian companies Act relating thereto and more particularly sections 93 to 96, which are summarised as below :—

A. PROSPECTUS ISSUED BY A NEW COMPANY .

1. Objects :

The contents of the memorandum, with the names, descriptions and addresses of the signatories and number of shares subscribed by each of them.

2. Directors :

- (i) The names, descriptions and addresses of the directors.
- (ii) The share qualification and remuneration of directors.
- (iii) Their direct or indirect interest in the promotion of or the property to be acquired by the company.
- (iv) The restrictions imposed by the Articles on their managerial powers.
- (v) The dates of and the parties to every contract regarding the appointment and remuneration of a managing director and the time and place at which it may be inspected.

3. Managing Agents :

- (i) The names, addresses and descriptions of the managers and managing agents.

(ii) Any provision in the articles or in any contract relating to their appointment and remuneration.

(iii) The commission or discount payable to them on shares.

(iv) The dates of and parties to every contract regarding their appointment and remuneration and the time and place at which it may be inspected.

4. Share Capital :

(i) The number of founders (or management or deferred) shares, if any, and the nature and extent of the interest of the holders in the profits and property of the company.

(ii) The number of redeemable preference shares with particulars of redemption.

(iii) The rights of other classes of shares.

(iv) The amount payable on application and allotment on each shares

(v) The minimum subscription.

(vi) The names of underwriters and the commission payable to them.

(vii) Any commission payable on shares or debentures and any discount on shares.

5. Property Purchased :

(i) The amount of the purchase consideration specifying the amount paid for goodwill.

(ii) The profits of the purchased concern for the last three years along with a recent balance sheet duly attested by the report of the accountant and the valuer respectively.

6. Vendors :

(i) The names and addresses of the vendors and the amount payable to each in cash, shares or debentures.

(ii) The shares issued for consideration other than cash.

7. Promoters :

(i) The amount paid or intended to be paid to any promoter, and.

(ii) The consideration for such payment.

8. Preliminary Expenses :

The amount or estimate of preliminary expenses.

9. Material Contracts :

The details of material contracts and the time and place where the same can be inspected.

10. Auditors :

The names and addresses of the auditors.

B. PROSPECTUS ISSUED BY A COMPANY ALREADY CARRYING ON BUSINESS

The Matters numbered 1, 2 (i, ii, iii), 3, (i) and 8, which are required to be disclosed in the prospectus of a newly-formed company are NOT required to be stated in the prospectus of an existing company; but in addition to the remaining information, a company already carrying on business prior to the issue of the prospectus must disclose the following additional information :—

(i) The amount of shares offered on each previous allotment within the past two years and the amount paid on the shares allotted.

(ii) Any commission on shares or debentures and any discount on shares paid during the past two years showing separately the amount so paid to managing agents.

(iii) Shares issued for consideration other than cash in the last two years, and the consideration therefor.

(iv) The amount paid to a promoter in the past two years and the consideration for such payment.

(v) The details of material contracts and the time and place of their inspection, and.

(vi) An auditor's report and an accountants' report showing the following particulars :—

(a) The profits of the company including its subsidiaries so far as the information is available in each of the three financial years immediately preceding the issue of the prospectus, the rates of dividend paid by the company on each class of shares for each of the said three years, and.

(b) The profits of the business proposed to be purchased for each of the three financial years preceding the issue of the prospectus.

C. PROSPECTUS ISSUED BY A PRIVATE COMPANY ON BECOMING PUBLIC

When a private company wishes to become a public company it must first alter its Articles and issue a prospectus containing all the particulars required to be disclosed in the prospectus of a newly-incorporated company except the amount or estimate of preliminary expenses.

D. PROSPECTUS ISSUED BY A FOREIGN COMPANY

When a foreign company issues a prospectus, it should contain particulars regarding the objects of the company, the instrument constituting or defining the constitution of the company, the law under which the company is incorporated, the address in British India where the said instrument or copies therefor can be inspected; the date on which and the country in which the company was incorporated; the address of the principal office of the company in British India; the auditors' report and the accountants' report as required in the case of a company registered in British India; the nature of liability of the members.

CONSEQUENCES OF OMISSIONS AND MIS- REPRESENTATIONS IN THE PROSPECTUS

Effect Of Omissions :

If a prospectus does not contain all the information required by law under section 93, every person who is responsible for it issue, shall be liable to a fine not exceeding Rs. 50/- a day so long as the default continues. Section 93 (5) further provides that nothing in that section shall limit or diminish any liability which any person may incur under the general law.

It should also be noted in this connection, that a person, who purchases shares or debentures on the faith of a prospectus containing some omissions, has no right to rescind the contract to take shares nor has he any other remedy against the company. However, if he has suffered a loss, he has a right of action for damages against the promoters, directors, or other persons responsible for the issue of the prospectus. The promoter, director or other person responsible for the prospectus shall not be liable, for non-compliance, if he can prove :—

(a) That they were not cognisant of any matter not disclosed.

(b) That the non-compliance or omission was due to an honest mistake of fact on their part; or.

(c) That the omission referred to matters immaterial which in the opinion of the court were capable of being excused.

Effect Of Misrepresentation :

Misrepresentation is a question of fact to be determined on the facts of each case. In considering what is misrepresentation, it is necessary to tell not only the truth, but all the truth and that

concealment of facts will amount to fraud. Two remedies are available for a shareholder who has subscribed for shares on the faith of a prospectus which contains some mis-statements of material facts :—

- (i) Right of Rescission and.
- (ii) Right of Action for Damages.

1. Right Of Rescission :

If any subscriber is induced to purchase shares on the basis of a prospectus containing misleading statements, the contract shall be Voidable at the option of the allottee, and he shall be entitled as against the company to repudiate his contract to take the shares and to have his name removed from the register of members and to recover the amount which he has already paid. Under sec. 19 of the Indian Contract Act., the contract would not, however, be voidable if the allottee had the means of discovering the truth with ordinary diligence.

THE RIGHT OF RESCISSION IS LOST :—

(i) If the shareholder does not take action within a reasonable time after the untrue statement has come to his knowledge; or.

(iii) If he impliedly ratifies the voidable contract after he has knowledge of any untrue statement, e g, by paying calls, receiving dividends or voting at company meetings goes into liquidation before the right of rescission is exercised.

2. Right Of Action For Damages :

The second right of a subscriber is to file a suit for damages against those responsible for the issue of the prospectus, and this right is available even after a company has gone into liquidation. Section 100 in this connection provides that a director or promoter is liable to compensate any person or persons who subscribe for shares or debentures on the faith of the prospectus for loss or damage sustained by them on account of any misleading or untrue statement appearing therein.

In an action for damages against the company, the subscriber must prove :—

- (i) That the company was responsible for the prospectus.
- (ii) That the prospectus contained misstatement of facts.
- (iii) That the misrepresentation was material.
- (iv) That he took shares on the faith of prospectus, and.
- (v) That as a natural consequence he has suffered a loss.

It should also be noted that compensation shall not be payable to any subscriber, if it is proved :—

(a) That the director or other officer had reasonable ground for believing the statement to be true, or.

(b) That having consented to act as a director, he withdrew his consent prior to the issue of the prospectus or.

(c) That he gave public notice, that it was issued without his consent or knowledge; or

(d) That he gave Public notice to withdraw his consent thereto with reasons, after the issue of prospectus but prior to the allotment of shares; or

(e) That he made the statement on the authority of an expert, whom he believed to be competent; or

(f) That the statement was a correct copy of some official extract.

The right of action for damages must be exercised within three years from the allotment of shares. A promoter or director who pays damages to a shareholder is entitled to a prorata contribution from his co-promoters or co-directors who would have been liable to damages. Moreover, the estate of a person who is liable under section 100 before death is not liable unless it has benefited by a misrepresentation contained in the prospectus.

Offer For Sale :

If a company allot or agrees to allot its shares or debentures to another company, firm or person, with the intention that, such company, firm or person may offer the same to the public; the document by which the shares and debentures so allotted are offered to the public is known as an "Offer for sale", and is deemed to be a prospectus under section 98—A. An offer for sale must disclose all the matters required to be disclosed in a company prospectus. Moreover, a copy of it must be dated and filed with the Registrar like a prospectus. It must bear the signatures of the persons making the offer. If the offer is made by a firm, it must be signed by at least half the partners and if it is made by a company, it must be signed by not less than two directors. An offer for sale must also contain the following additional information :—

(i) The net amount of consideration received by the company in respect of the shares or debentures to which the offer relates, and.

(ii) The time and place at which the contract for the allotment of the said shares or debentures may be inspected.

It is, however, possible in an offer for sale to add exaggerated or misleading statement relating to the company by simply stating at the top of such an advertised announcement some such words as, "This is not a prospectus but simply an announcement". Such announcements serve as an invitation to the public to subscribe for shares or debentures on the faith of the exaggerated or misleading statements contained therein. A large number of such announcements have appeared in the press during the war-boon period from 1939 onwards. As already remarked, such trade announcements are out of the province of sec. 2 (1) clause 14, defining a company prospectus. This is a great weakness of the law from the point of view of prospective investors, because there are no restrictions as to the contents of such advertisements they may contain exaggerated statements which might mislead the general public. Moreover, it may be that the companies might not have issued any prospectus at all.

Statement In Lieu Of Prospectus :

A public company which does not issue a prospectus on its formation, cannot allot any of its shares or debentures unless it issues a statement in lieu of prospectus and files the same with the Registrar duly signed as required by section 98. The object of such a statement is to give publicity as to the essential matters of its constitution. It must contain the information prescribed in Form I and Form II given in the Second Schedule of the Act, which may be summarised as below :—

(i) Particulars of share capital, i. e., amount and number of shares, whether they are redeemable, particulars of redemption, rights attached to the different classes of shares etc. etc.

(ii) Consideration for the property purchased.

(iii) Particulars of underwriting.

(iv) Particulars of directors and managers and the remuneration payable to them

(v) The amount of preliminary expenses. Effect of untrue statement in lieu of prospectus :—

The Indian companies Act is silent as to the liability arising from untrue statements in the statement in lieu of prospectus, but,

on general principles of law, if such document contains a false statement, a person buying shares on the faith of that statement may have a right to rescind the contract, though a person who had not seen the statement before he took the shares or who did not rely thereupon while taking the shares would have no grievance and cannot claim rescission. Inaccuracies, mis-statements or omissions in the statement in lieu of prospectus do not, however, vitiate an allotment, and a company can proceed to allotment notwithstanding misstatements and omissions contained therein.

Section 100 does not apply to a statement in lieu of prospectus, and hence the person aggrieved would not be entitled to compensation under this section, though he would be entitled to damages under the general law for deceit and in having acted on the faith of misleading or untrue statement contained therein. Besides, a person responsible for the issue of a statement in lieu of prospectus, would expose himself to a criminal liability under sec. 282 of the Act.

CHAPTER III.

MEMBERSHIP AND CAPITALISATION

WHO ARE MEMBERS ?

Under section 30, the members of a company can be divided into two categories :—

(i) Those who are subscribers to the memorandum. They are deemed to have agreed to become members of the company and as soon as the company is registered, they are entered as such in its Register of Members; and

(ii) Those have agreed to become a member and whose name is entered in its Register of Members.

A person may become a member of a company in any of the following ways :—

(1) By subscribing to the Memorandum before its registration:—In the case of subscriber to the Memorandum, no allotment

is necessary, as he is bound to take the shares from the company to the extent mentioned in the memorandum and to pay for them on the calls duly made. He cannot repudiate his liability on the ground of misrepresentation or on the ground that his name did not appear on the Register

(2) By application and allotment—A person who applies for a certain number of shares becomes a member, when the shares are allotted to him and his name is entered in the Register of Members. The general law of contract applies to this transaction. Thus it is not the agreement alone that would create the status of membership, but the shareholder's name should also be entered in the Register of Members before such status can be acquired. To constitute an agreement, there must be an application by the intending shareholder and allotment by the directors of the company, followed by a communication to the applicant of the fact of such allotment having been made. An applicant is also entitled to withdraw his application before the allotment is actually made by the directors. Withdrawal may be made verbally or in writing. Again, an application may be made by an agent duly authorised by the applicant in that behalf and may similarly be made to an agent of a company duly authorised to receive such application.

(3) By Transfer of Shares—A person taking a transfer of shares becomes, subject to Articles, entitled to be registered as a transferee and placed on the Register of Members in place of his transferor.

(4) By operation of law—A person may become a shareholder by registration if he succeeds to the estate of a deceased shareholder, e.g., an official receiver or assignee is entitled to become a member in place of a member who is declared as an insolvent.

(5) By estoppel—If a person elects to remain on the Register of Members even when his name has been improperly entered thereon, he may be deemed to be a member of the company on the principles of acquiescence and in such a case he may be estopped from denying that he is registered with his consent.

(6) By delivery of share Warrants—If the articles so provide a director appointed by the articles who signs and delivers to the Registrar a written undertaking to take and pay for his qualification shares is deemed to be a member though not registered.

Who may be members ?

(1) Any person *sui juris* (i. e., capable of entering into a contract) can become a member.

(2) A foreigner or an insolvent or a married woman can be a shareholder.

(3) An infant or a minor cannot become a member unless he becomes entitled to shares by operation of law e. g., by inheritance.

(4) On the same principle given in rule No. 1 a lunatic cannot be a member of a company.

(5) A corporation being a juristic and competent to enter into an agreement can become a member, if it is authorised to hold shares in a company under its constitution.

(6) A firm cannot become a shareholder as it has no existence in law. If, however, the name of the firm is, by an oversight, entered in the Register of Members its partners are deemed to become members of the company. On the same principles, a trust cannot become a member, though the shares may be registered in the name of the trustees in whom the property of the Trust vests.

Cessation of membership :

A person will cease to be a member of a company in the following cases :—

(1) When he transfers his shares and the transfer is duly registered in the books of the company.

(2) When his shares are validly forfeited or when he surrenders his shares to the company. (In both these cases he is liable as B list contributory, if sale or forfeiture takes place within one year of winding up).

(3) When his shares are sold by the company under a provision of its articles e. g., for its lien.

(4) When he dies (his estate remains liable until some one else is registered as a member.

(5) When the official assignee or the Receiver in Insolvency of an insolvent member disclaims his shares.

(6) When he rescinds the contract of membership on the ground of fraud, mistake or misrepresentation (a subscriber to a Memo cannot avail of this right).

(7) When the company is wound up (In this case the shareholder will cease to be a member but he will remain liable as a

contributory and is also entitled to his share in the surplus assets, if any).

(8) When the member avoids the allotment, where the minimum subscription is not subscribed.

(9) When he exchanges the shares with bearer Warrants.

(10) On the redemption of redeemable preference shares.

SHAREHOLDER AND MEMBER DISTINGUISHED

SHAREHOLDER	MEMBER
1. The person who holds a share warrant to bearer is a shareholder.	1 The share-warrant holder is not a member till his name does not appear on the Register of Member.
2. The legal representative of a deceased or insolvent member is a shareholder even without being placed on the Register of Members.	2. The legal representative of a deceased or insolvent member is not a member until he applies to the Company for registration as a member.
3. Only the share-warrant holder is a shareholder; he may or may not be a member.	3. Ordinarily, a member must also be a shareholder first; but this term member does not include every shareholder. Moreover in the case of guarantee companies not having a share capital it includes people who hold no shares at all.

Rights of members :

The member of a company have got the following rights :—

- (1) To receive the notice of allotment of shares.
- (2) To get the share certificates within three months of allotment or transfer.
- (3) To have their names on the register, as also to inspect or make extracts from the register and have it rectified.

(4) To transfer shares of course, subject to the provisions of articles.

(5) To attend company meetings, to have proper notices and to vote at meetings.

(6) To have copies of Memorandum and Articles on request and payment of the prescribed fees.

(7) In the case of a further issue of shares by the company, to have as existing members a first chance to purchase the new shares.

(8) To have the statutory report, a just balance of profit and loss and the balance sheet duly audited by auditors along with their report.

(9) If articles are not registered, to have on request copies of special resolutions passed by the company.

(10) To have on request, minutes of proceedings at general meetings and of proceedings at directors' meetings.

(11) To control the directors and managing agents and to remove by an extra ordinary resolution a director who is subject to retirement before the expiry of his period of office, and appoint by ordinary resolution, another person as director.

(12) To approve assignment of office by directors.

(13) To approve by a resolution at a general meeting the appointment or removal of managing agents or the variation of managing agents' contract of management.

(14) To stop the managing agent from assigning his office.

(15) To apply for the appointment of Inspectors by the Central Government to investigate into the affairs of the company.

(16) To appoint by special resolution inspectors to investigate into the affairs of a company.

(17) To appoint auditors at the annual gathering of the members.

(18) To have a share in the capital of the company and in the surplus assets, if any.

(19) To resolve by a special resolution for the winding up of the company voluntarily or by Court, and

(20) To appoint, fix the remuneration of one or more liquidators in case of Members' Voluntary winding up, and to fill vacancy in the office of liquidator so appointed by them.

CAPITALISATION OF A COMPANY

After the incorporation of a company, the next important thing for the promoters is to secure the necessary amount of capital, which may be arranged privately or by an invitation to the public to subscribe for shares &/or debentures.

Share Capital :

According to section 2 (16), a 'share' means "a share in the capital' of a company." Farewell J. has defined a share as "the interest of a shareholder in the company measured by a sum of money, for the purpose of liability in the first place and of interest in the second but also consisting of a series of mutual covenants entered into by all the shareholders inter se." The share capital of a company is the money subscribed by the shareholders for the purposes of the company. It may be sub-divided into following categories.

1. **Nominal Registered or Authorised Capital :—**This is the amount with which the company proposes to commence its business, and which is specified in the Memorandum. The nominal capital is sub-divided into shares, each of so many rupees.

2. **Issued and Subscribed Capital :—**It means the capital which is actually allotted to the shareholders, i. e. which is issued by the company and subscribed by the shareholders. Generally speaking there is no difference between the terms issued and subscribed capital; but if some of the allotted shares are forfeited for non-payment of calls, difference will have to be made between these terms. Under such circumstances, the terms issued capital' will mean the total number of shares allotted by the company, while the term 'subscribed capital' will stand for the actual number of shares forfeited.

3. **Called up Capital :—**A company does not usually require the full nominal amount of the shares all at once, and it, therefore, calls up the amount according to the requirements. The amount of money called up on the shares actually issued is known as the "called up capital,"

4. **Paid up Capital :—**It stands for that part of the called up capital which is actually paid by the shareholders. Naturally, therefore, the amount of paid up capital will be less than the called up capital, if some of the shareholders fail to pay the calls made upon their shares. The difference between the called up and the paid up capital is known as "CALLS IN ARREAR."

5. Reserve Capital :—If a company decides by special resolution that a certain portion of its called capital shall not be capable of being called up except in the event and for the purposes of liquidation, such portion is known as 'Reserve Capital'. (section 69).

It should also be noted in this connection that along with the advertisement for the authorised capital, a company must also advertise side by side the amount of its issued and subscribed capital, otherwise the company and its officers shall be liable to a fine not exceeding Rs. 1,000/- (Section 75).

Classes of Shares :

Shares are of various classes ; the following are however their common varieties :—

1. Preference Shares :—Preference shares are those the holder of which is entitled to some preferential rights over other classes of shares, viz ; they will stand first in the queue of dividend-takers, i. e., other classes of shareholders will get their share of the dividend only after a fixed sum has been paid to the preference shareholders out of the profits of each year. In most of the cases they also possess the right to a return of capital in priority to other classes in the event of the company's winding up. Again, the preference shares may be classified into following categories.

(a) **Simple or Non-cumulative Preference Shares :—**The non-cumulative preference shares give a right to a fixed percentage as dividend out of the profits of each year ; and where no profits are earned, the holders get nothing nor can they claim unpaid dividend in subsequent years.

(b) **Cumulative Preference Shares :—**Such share gives a right to demand even the unpaid dividend in any year. Thus if the dividends are not paid in any year due to absence or insufficiency of profits, it will go on accumulating till the entire sum is paid. A preference share is always cumulative unless otherwise stated.

(c) **Guaranteed Preference share** is one in respect of which the dividend and repayment of capital are guaranteed by another company. They are usually issued where a private concern is turned into a limited company or where one company is sold to another company. The vendors or any other interested party in

these cases, guarantees a specified rate of dividend for a number of years.

(d) Participating Preference Share is one which possesses the right to a fixed dividend, and, in addition, entitles the holder to participate in the surplus profits, if any, after the ordinaries have received a dividend at the fixed rate,

(e) Convertible Preference share is one which is capable of being converted into any other class of shares within a specified period.

(f) Redeemable Preference Shares are those which can be redeemed out of the profits which would be available for dividend or out of the proceeds of the issue of new shares. The shares must be fully paid before they can be redeemed. For this purpose Capital Redemption Reserve Fund is to be created which is utilised at the due time of redemption in order that it might not result in any reduction of capital.

3. Ordinary Shares :— Ordinary shareholders do not possess the right to a fixed dividend or to repayment of capital. They receive their dividend out of profits as determined by the directors and declared by the shareholders at their general meeting, after making due allowance for 'depreciations' 'reserve' etc. The rate of dividend on ordinary shares varies according to the amount of profits available.

4. Deferred, Founder's or Management Shares are those that rank for dividend after all the other classes of shares have received fixed rates of dividend. The payment of dividends on these shares is postponed or deferred, hence this name; they are frequently taken up by the promoters—the founders—and/or those connected with management and hence are sometimes designated as "Founder's or Management Shares". Generally they are few in number and have small nominal value, but the voting rights which they command are the profits to which they are entitled are often considerable.

5. Qualification Shares are those which, according to articles, must be held by every director before he can act as such.

DISTINCTION BETWEEN SHARES AND STOCK

SHARE	STOCK
1. A 'share' means a share in the share capital of the	1. Stock is a set of fully paid up shares put together.

company and includes 'stock'. A share has a nominal value which is the total amount the holder is liable to contribute to the capital of the company, and it confers upon the holder the right to participate in the company's profits and its assets on winding up. Shares need not necessarily be fully paid up.

2. Shares are transferable as a whole.

3. Shares can be issued directly to the shareholders.

2. Stock is transferable in sums of any amount.

3. Stock cannot be issued directly, but only after the conversion of its fully paid shares into stock. If the articles so authorise, it can be done under sec. 50. Where a company has converted its shares into stock, a notice of such conversion must be filed with the Registrar within one month.

As regards the difference between share and stock, Lord Cairns has pointed out in *Morrice V. Aylmer* —

"The use of the term stock merely denotes that the company have recognised the fact of the complete payment of the shares and that the time has come when the shares may be assigned in fragments which for obvious reason could not be permitted before but that stock shall be a qualification e. g. of directors who must possess certain number of shares and that the meeting shall be of persons entitled to this stock who meet and vote as shareholders in the proportion of shares which would entitle them to vote before the consolidation into stock."

Allotment of Shares :

The term "allotment of shares" means an appropriation by the directors or the managing body of a certain number of shares in response to an application. It is, in fact, an acceptance by the company of the offer to take shares and creates a binding

contract between the company and the applicant. Like any other acceptance of an offer, allotment must be both unconditional and communicated. Allotment of shares remain merely a contract until the particular allottee is registered in the register of Members, after which he will become a member of the company. The allotment of share must be made within a reasonable time from the date of application otherwise the applicant is not bound to accept it. The Indian Companies Act requires certain conditions to be fulfilled before a PUBLIC company can proceed to allot shares ; there are, however, no restrictions on a private company as regards the allotment of its shares. These conditions are given in section 101 and may be studied conveniently under two heads :—

1. Allotment of Shares in the case of a Prospectus :—

Issue Company :

In the case of a prospectus—issuing company, no allotment of shares can be made, unless the following conditions are satisfied :—

1. The minimum subscription as laid down in the prospectus has been subscribed for. The term "minimum subscription" here means the amount which in the opinion of the directors, must be raised from the public by means of shares in order to provide the sum required for the under-mentioned purposes —

(i) The purchase consideration of any property to be met out of the proceeds of the issue.

(ii) Working capital.

(iii) Preliminary expenses and underwriting commission ; and

(iv) Repayment of money borrowed for these purposes.

2 At least 5% of the minimum subscription (as defined above) has been received in cash.

3, All the monies received from applicants should be deposited and kept in a Scheduled Bank until the certificate to commence business is obtained by the company under sec. 103 or it should be returned to the applicants in accordance with the following provisions.

4. If the allotment is not made within 180 days, the money received must be returned within 190 days without interest ; and if it is not so returned, the directors will be jointly and severally liable to repay the money with interest at 7% from 190th day, provided that a director shall not be liable if he proves that the loss of money was not due to any misconduct or negligence on his part.

11. In the case of a Non-Prospectus Issuing Company:

In the case of a non-prospectus issuing company, no allotment can be made, unless the following conditions are satisfied :—

The minimum subscription is subscribed for. The term 'minimum subscription' here means either (i) the amount, if any fixed by the memorandum or articles and named in the statement in lieu of prospectus as the minimum subscription on which the directors may proceed to allotment ; or (ii) if no amount is so fixed, and named, the whole of the share capital payable in cash.

2. A statement in the lieu of prospectus has been filed with the Registrar.

3. At least 5 p. c of minimum subscription (as defined above) should be received in cash.

Return of Allotment :

After the completion of allotment, the directors are required to file within a month of allotment, a "Return of Allotment stating the number and nominal amount of shares allotted, the names, addresses and descriptions of the allottees, and the amount paid, treated as paid or due and payable on each share (section 104). If the shares are allotted for consideration other than cash. (e. g., in exchange of Plant, Machinery or Buildings purchased), the Registrar is authorised to inspect and examine all contracts by which the allottees become entitled to the shares so allotted.

Irregular Allotment and its Effect :

An allotment of shares made in contravention to the provisions of section 101 is known as "Irregular Allotment". The consequences of irregular allotment are as below .—

(i) An irregular allotment shall be voidable at the option of the applicant within a month after the holding of the statutory meeting, or where the allotment is made after the holding of the statutory meeting, within one month after the date of the allotment and not later. The allotment shall be voidable even if the company goes into liquidation.

(ii) Any director of the company who knowingly contravenes shall also be liable to compensate the company and the allottee respectively for any loss or damage or costs which the company or the allottee may have sustained or incurred thereby, provided that the proceedings to recover such loss shall not commence after the expiration of two years from the date of allotment.

Commencement of Business :

Though a company becomes a legal entity on incorporation, it cannot (except when it is a private company without a share capital) commence any business or exercise any borrowing power unless all the following conditions in section 103 are first complied with :—

(1) Shares not less than the minimum subscription to be paid in cash must have been allotted

(2) Every director of the company has paid to the company on each of the shares taken or contracted by him, and for which he is liable to pay in cash, a proportion equal to the proportion payable on application and allotment on the shares offered for public subscription.

(3) There has been filed with the Registrar a duly verified declaration by the secretary or one of the directors that the above requirements have been complied with.

(4) There has been filed with the Registrar a statement in lieu of prospectus in the case of a non-prospectus issuing company.

When these conditions are complied with, the Registrar shall certify, on the filing of the duly verified declaration as aforesaid, that the company is entitled to commence business and such certificate shall be conclusive evidence that the company is so entitled;

Non-compliance of these provisions shall render every person responsible for the contravention to fine not exceeding Rs. 500/- for each day during which the contravention continues (section 103 sub sec. 5).

These restriction on the commencement of business does not, however, mean that company may not enter into any contract unless the provisions of sec. 103 are complied with ; the company can, nevertheless, make contracts in respect of its intended business even before the date at which it is entitled to commence business. Such contracts shall, however, be provincial only and shall not be binding on the company till the date aforesaid, but shall become binding on that date (sec. 103 sub sec. 3).

Share Certificate :

A share certificate is a document of title to the shares held in a company, issued under its common seal and states (i) the

name and address of the holder ; (ii) the number of shares held by him ; (iii) the distinctive numbers of shares and (iv) the amount paid on the shares. A share certificate is a prima facie evidence of the title of the members to the shares specified therein (sec. 29), though it does not give the person an absolute or an indefeasible right to the shares. Accordingly if it may be shown that the shares were acquired by the holder from some person who could not give the title to them, the name of the true owner will be retained upon or restored to the Register of Members*.

Under the law, every shareholder is entitled to get a share certificate from the company in which he holds shares. This is to give him his opportunity of more easily dealing with his shares in the market and to afford facilities to him of selling those shares by at once showing a marketable title. According to Indian Stamp Act, a share certificate must bear a uniform duty of Rs. -/2/- per share certificate.

Under Section 108, a share certificate must be ready for delivery within three months after the allotment or registration of transfer, unless the terms of issue provide otherwise. If this condition is not complied with, a penalty not exceeding Rs. 50/- a day may be imposed so long as the default continues.

Generally, a shareholder is entitled to one certificate, free of charge, and upon payment of a small fee and the execution of an indemnity bond such a certificate may be replaced, if it is 'defaced, lost or destroyed. The articles may also provide for the issue of more than one share certificate.

If the shareholder acquires the shares in good faith and for value on the faith of and in exchange for a certificate issued by the company, the company will be estopped from denying his title to the shares which he was induced to buy or pay for by being shown in the certificate. The holder can, in such a case, only claim damages against the company and is not entitled to the shares as against the true owner. Where it is stated in the certificate that the shares are fully paid up, or partly paid up, and a person, acting on the faith thereof, purchases the same, the company or its liquidator is estopped from alleging the con-

* Vide "Company Promotion and Management" by A. N. Khanna
Page 67.

trary, though a person who knew that such shares were not fully paid up, cannot take advantage of the statement in the certificate. There is however, no estoppel, if the certificate is a forgery.*

Share Warrants :

A limited company (except a private company) may, if so authorised by its articles, issue with respect to any fully paid up share or stock, a warrant under its common seal stating that the bearer is entitled to the shares or stock specified therein, and may provide by coupons or otherwise for the payment to future dividends on the shares or stock included in the warrant. Such warrant is known as a "Share Warrant," and it entitles the holder to the shares or stock specified therein which may be transferred by mere delivery (section 43 and 44). Thus even if it has been previously stolen a subsequent innocent purchaser for value gets a good title to it.

The bearer of the share warrant if so authorised by its articles may surrender it for cancellation in order to have his name entered as a member in the Register of Members (sec. 45). If the articles of a company so provide, the bearer of a share warrant may be deemed to be a member of the company, either to the full extent or for any other purposes defined in the articles. (sec. 46). On the issue of share warrant, the company shall strike out of its register of members the name of the member then entered therein as holding the shares or stock specified in the warrant as if he had ceased to be a member and shall enter in the register the following particulars :—

- (i) the fact of the issue of warrant ;
- (ii) the date of the issue of the warrant ;
- (iii) a statement of the shares or stock included in the warrant distinguishing each share by its number (sec. 47),

Until a warrant is surrendered the above particulars shall be deemed to be the particulars required by the Act to be entered in the Register of Members and on a surrender, the date of surrender, shall be entered as if it were the date on which a person ceased to be a member (sec. 48).

* Vide "Company Promotion and Management" by A. N. Khanna

DIFFERENCES BETWEEN A SHARE WARRANT AND A SHARE CERTIFICATE

SHARE CERTIFICATE	SHARE WARRANT
1. A share certificate is issued to every person to whom shares have been allotted.	1. Share warrant can be issued only in respect of fully paid up shares or stock.
2. The shares here can be transferred only by means of a properly executed transfer deed.	2. The shares stated in a share warrant can be transferred by a mere delivery of the warrant.
3. The name of the holder of a share certificate appears in the company's register of members.	3. The name of the bearer of a share warrant does not appear in the register of members.
4. The shares stated in a share certificate constitute share qualification required for a director.	4. The shares mentioned in a share warrant do not so constitute.
5. The holder of a share certificate is a member of the company.	5. The bearer of a share warrant is not a member unless the articles of the company so provide.
6. The holder of a share certificate can present a winding up petition.	6. The bearer of a share warrant cannot do so.

Commission on Shares :

According to section 105, a company is entitled to pay commission out of capital to any person who subscribes or agrees to subscribe, procures or agrees to procure subscription for shares in the company subject to following provisions :—

(i) That the payment of the commission be authorised by the articles.

(ii) That the rate of commission must not exceed 10 p. c. of the issue price or any less rate specified in the articles; and

(iii) That the amount or the rate of commission payable must be disclosed in the prospectus or statement in lieu of prospectus or in a statement in a prescribed form to be filed with the registrar.

These requirements apply only where any shares or capital monies of the company are applied in the payment of the commission, and particulars of any sums so paid must be disclosed in every Balance Sheet of the company, until the amount has been written off. Further, these provisions do not affect the payment of brokerage which it is customarily lawful to pay. No formalities are necessary if the commission is paid out of profits.

The commission on shares may be paid to underwriters procurers of persons to take shares, and also to persons taking shares. The commission which is paid to the underwriters is known as "UNDERWRITING COMMISSION". Underwriting is a method of sales insurance whereby the underwriters agree, in consideration of some commission, either to purchase a specified number of shares or debentures of a company in bulk for resale later or to purchase any balance of such securities not taken up by the public. Underwriting differs from the "Placing of Shares" in as much as a person who agrees to place shareholder himself in case he fails to sell the stipulated number of shares. The underwriter is liable to take over the unsubscribed shares, and the person who fails to place shares is liable only for damages.

Issue of shares at a discount :

The issue of shares at a discount was held to be void on the principle that any arrangement by which the liability of a shareholder to pay the nominal amount of the share acquired by him in a company is excused to any extent is invalid. Section 105—A of the Act recently added by the amending Act of 1936, however, validates the issue of shares at a discount. According to this section, it is now lawful for a company to issue its shares of a class already issued at discount subject to the under-mentioned restriction :—

- (1) The shares are of a class already issued.
- (2) The issue is authorised by resolution passed in general meeting of the company and is sanctioned by the court.
- (3) The resolution must specify the maximum rate of discount (not exceeding 10 p. c. in any case) at which shares are to be

(4) Such an issue can take place only after at least a year from the date at which the company was entitled to commence business.

(5) The issue must be made within six months after the date of the court's sanction.

(6) The particulars of the discount allowed on the issue of such shares or so much of the discount as has not been written off, must be stated in every prospectus and balance sheet issued subsequently to the issue of such shares.

In the case of default, the company and every officer of the company who is in default is liable to a fine not exceeding Rs. 50 -.

Redeemable preference shares :

According to section 105—B, if authorised by its articles, a company limited by shares may issue preference shares which are, or at the option of the company are to be, liable to be redeemed. The following are, however, some restrictions on the redemption of preference shares :—

(1) No such shares can be redeemed unless they are fully paid.

(2) No such shares shall be redeemed except out of profits of the company which would otherwise be available for dividend or out of the proceeds of a fresh issue of shares made for the purpose of the redemption or out of sale proceeds of any property of the company.

(3) Where preference shares are to be redeemed out of the proceeds of a fresh issue of shares, there is no restriction except that any premium payable on redemption must be provided out of profit before the redemption.

(4) Where the redemption of preference shares is made out of profits available for dividends or out of the sale proceeds of any property, there must be transferred out of such profits to a "Capital Redemption Reserve Fund" a sum equal to the amount applied in effecting the redemption. This capital redemption reserve fund is incapable of being used for revenue purposes, nor can it be used for normal capital purposes such as writing off share and debenture, discount, goodwill etc. This fund also cannot be reduced except in accordance with the rules relating to the reduction of share capital

(5) Particulars of all redeemable preference shares must be disclosed in every balance sheet of the company.

Right of pre-emption :

The right of pre-emption (i.e., purchasing something before others) is provided by section 105—C. According to this section, where the share capital of a company is increased by the directors (i.e., by issuing the unissued shares), such shares must in the first instance be offered to the existing shareholders (irrespective of class) proportionately to their existing holdings. In other words the shareholders are given a statutory right of pre-emption, which is a valuable privilege in the case of successful companies.

Where, however, the authorised capital of the company is increased by the creation of new shares, the shareholders of the company have no statutory right of pre-emption in respect of them. But such right may be conferred either by the company's articles or by the company's resolution passed for increasing the authorised capital.

CHAPTER IV.

CALL, FORFEITURE, SURRENDER ETC.

What is a call ?

Members of a company are liable to pay to the company to the extent of the nominal amount of their shares. Usually they are required to pay a certain amount (not being less than 5 per cent of the nominal value of a share as required by section 101) on application, a further sum on allotment, and the balance is either made payable at some subsequent fixed date or the shares are left partly paid; and this payment is made on a demand from the side of company directors. Such demand is technically known as what we call a "CALL" which really means the application to the shareholder to pay and the amount to be paid.*

* "Indian Mercantile Law" by M. C. Shukla Page 268.

"Shares are generally issued to the public so that a Rs. 100/- share is made payable thus; Rs. 10/- on application, Rs. 20/- on allotment; another Rs. 20/- in two months' time, and the remaining Rs. 50/- as and when called for. The first two and according to *Croskey V. Bank of Wales* (1863) 4 Giff. 314 also the third are not "CALLS" but when the company calls upon the shareholders to pay the whole or part of Rs. 50/- the directors make a CALL. So, a CALL may be defined as a demand by the company on its shareholders to pay the whole or part of the balance still payable on each share made at any time during the continuance of the business. It may also be made by the liquidator in the course of the winding up of the company.

Kinds of a call :

There are two kinds of call. First of these are those which are nothing more than unpaid portions of the nominal capital of a company; and secondly, there are those calls which are contributories required. Calls of the first kind are payable by virtue of the agreement entered into by the subscribers and the shareholders to contribute the sum fixed upon as the capital, but calls of the last kind are payable in consequence of the liability of shareholders to discharge their debts. If this liability is unlimited, the amount of calls (of the second kind) which a shareholder may be compelled to pay depends entirely on the amount of the debts to be liquidated and upon the number of the solvent shareholders. But no shareholder can be required to pay calls of the first kind beyond his unpaid proportion of the capital of the company*.

Valid call :

Each shareholder is liable to pay a valid call. The conditions precedent for a valid call are :—

(i) That the persons acting as directors were duly appointed and duly qualified.

(ii) That there was a duly convened meeting of the Board of Directors.

(iii) That a proper quorum was present there at, and

(iv) That the resolution making the call was duly passed specifying the amount of call, the time and place of payment and to whom the call is to be paid.

*Lindley, *Law of Companies* 6th edition, Page 573—Quoted by A. N. Khanna in his "*Company Promotion and Management*" Page 97.

Call must be made on ALL holders of a class of shares, unless the articles provide otherwise; and must be paid in cash. The call is in the nature of a trust, and must be made only for the benefit of the company, and NOT for the private ends of the directors.

The power to make calls may be exercised by the directors unless it is expressly reserved to the company in general meeting.

In making calls, the requirements and formalities stated in the articles must be strictly followed :—

The liability for the payment of calls extend to the estate of a deceased member and accordingly if at the time of making the call the member is dead the call can be recovered out of his estate and the company can apply to have his estate administered by the Court. Likewise, on a member becoming insolvent, the company may prove in insolvency the uncalled liability on the shares but may also include in its proof an amount equal to the estimated amount of the future calls.

Payment of calls in advance :

Under sec. 49 (2), the company is empowered by the Act to receive payment of calls in advance. Such power is, however, in the nature of a trust and must be exercised only for the benefit of the company, i. e., the company can receive payments in advance only if the directors are of the opinion that it is necessary to accept such payments and that the money so received can be utilised advantageously for the purposes of the company. The company may also pay interest on the amount received in advance of calls and such interest must be paid whether there are profits or not. If there are no profits or if the profits are insufficient, the interest can be paid out of capital, and there is nothing ultra vires in it, the effects of payment in advance are as follows :—

(1) If the payment is made in advance and is received bonafide and in accordance with the provisions of the articles, the shareholders' liability in respect of their shares, both during the existence of the company and in the event of winding up, extinguishes protanto.

(2) Interest may be made even out of capital.

(5) Money paid in advance of calls cannot ordinarily be repaid to the shareholders except in the event of winding up.

FORFEITURE OF SHARES

The Indian companies Act is silent on the subject of forfeiture of shares. A company, therefore, is not empowered to forfeit the shares only if they are so permitted by the articles of the company. Where there is no such power under the articles, the articles may be altered by a special resolution so as to provide the directors with the requisite power. On this subject of forfeiture of shares, Shadi Lal, J., summarised the law in *Kanshiram V. Kishore Chand* as follows :—

“A right to forfeit shares must, in order to be effectually exercised, be used with the greatest exactness; it must be exercised by the proper purpose, i. e., by directors properly appointed and in the proper manner and for the proper cause. The right must be exercised bona fide for the purpose for which it was conferred. The power to forfeit is a trust the execution of which will be narrowly scanned by the court. It cannot, for example, be exercised surreptitiously, for the purpose of assisting him in getting rid of shares and retiring from the company is a fraud of the other shareholders. The court will not sanction or recognise as valid a forfeiture made mala-fide for any such purpose”.

Procedure of forfeiture :

The procedure of forfeiture is usually prescribed by the articles of a company; and the articles generally provide a power to directors to forfeit the shares in the event of non-payment of calls within a certain period after a proper notice has been served on the defaulters. A valid call and default are conditions precedent and necessary for a valid forfeiture. The procedure of forfeiture may, however, be analysed as follows :—

(1) A notice should be sent to the defaulting shareholders by registered post. The notice should state that unless the call due and interest and expenses are paid by a specified date, the share will be forfeited without prejudice to company's right to sue for calls due.

(2) On the expiration of the specified period, it is usual to send the peremptory notice that since the amount has not been paid forfeiture will follow.

(3) A formal resolution forfeiting the shares will then be passed by directors.

- (4) Notice of this resolution must also be sent to the defaulter.
- (5) The shares are then transferred to the shares' forfeited a/c.
- (6) Then the necessary entries are passed in the books of account.
- (7) An entry shall also be made in the defaulting members' a/c in the Register of Members and the date and number of resolution shall also be entered.

A forfeited share may be sold or otherwise disposed of on such terms and in such manner as the directors think fit, and at any time before a sale or disposition, the forfeiture may be cancelled on such terms as the directors may decide.

On forfeiture of share the defaulter ceases to be a member of the company and ceases also to be liable to pay any further money in the capacity as a shareholder. All that is left is his new liability to pay to company all moneys which at the date of forfeiture were presently payable by him to the company in respect of the shares. Where the articles entitle the company to sue for unpaid calls in respect of the forfeited shares after forfeiture and the shares are forfeited for non-payment of call, the shareholder is liable to pay the arrears of unpaid call as he becomes, in such case, a debtor of the company in respect thereof. The company can also in such a circumstance (when the payment in full is not made by any defaulter) sue the member for the amount of the unpaid calls.

A company is not entitled to interests on arrears of calls after forfeiture.

Cancellation of forfeiture :

The conditions for cancellation of forfeiture are—(i) That the articles of the company must confer on the directors power to annual forfeiture, and (ii) The directors can do only with the consent of the shareholders concerned, for if, once a valid forfeiture is effected, it cannot be revoked unless, of course, the concerned shareholders themselves agree to their names being replaced on the register of members.

Surrender of shares :

The surrender of shares means that a shareholder returns his shares to the company for cancellation. There is no reference in the Indian companies Act to the surrender of shares, but these have been admitted by courts upon the principle that they have

practically the same effect as forfeiture, the main difference being that one is proceeding in invitum and the other is a proceeding taken with the assent of the shareholder who is unable to retain and pay future calls on the shares. Therefore, company may, if authorised by its articles under certain circumstances accept a surrender of shares, namely, where :—

(i) It is in circumstances in which the shares could be forfeited, as a short cut to forfeiture by the avoidance of the formalities necessary for forfeiture, and

(ii) Fully paid shares are surrendered in exchange for new shares of the same nominal value.

As pointed out in Palmer's company Law, "a company may in certain cases accept a surrender of shares, e. g., as a short cut to forfeiture; but if a company proposes to take back shares which are repudiated on the ground of misrepresentation it seems doubtful whether the power to accept surrenders can safely be exercised, unless it is sanctioned by the court, or unless the company is in a position to forfeit the shares and bonafide arranges for a surrender as the short cut to the same end. The validity of each case must be decided on its own merits".

Pledge or mortgage of shares or stock :

There is a difference of opinion as to whether shares and stock would be 'goods' within the definition of sec. 172 of the Indian Contract Act, so as to be capable of pledge or mortgage. Their Lordships of the Calcutta High Court on this subject once observed as below* :—

"We think that when a person delivers a share certificate to another to be held by him as security, there is under the law of India pledge which, he can enforce, but unless the pledge at the time of deposit secures the deed of transfer which he can use in the case of necessity or obtains one from his debtor at a later stage, he must have recourse to court when he wishes to enforce his security".

Mortgage of shares is possible in two ways :—

1. **Legal Mortgage**—It can be made by transferring the shares to the lender. The transfer should be accompanied by a separate mortgage deed setting out the terms of the loan and providing that the shares shall be transferred back to the borrower

*In *Laht V. Haridas* (1916) 24 C. L. J. 335.

on payment of the debt and interest. The mortgage shall be entitled to receive dividends and to vote at company meetings :—

2. **Equitable Mortgage**—Here the share certificate may be deposited with the lender, whose remedy in the event of default in payment will be to apply to the court for a sale or for an order for the transfer of shares to him.

Lien :

Prima facie a company has no lien on the shares of its members; but the articles may and usually do provide that the company shall have first lien on the shares of each member for his debts and liabilities to the company. The Regulation 9 of Table A provides for lien on every share other than fully paid up one standing in the name of a member for all moneys payable thereon. Regulations 10 and 11 of Table A provide for the enforcement of such lien by a sale. Where the articles of a company do not provide for a lien, a lien clause may be adopted by a special resolution. Fully paid up shares can also be brought in so as to be subject to the lien by a proper alteration of the articles. A company has, however, no lien on the fees due to its directors.

The lien is an equitable charge and is transferable. A company is, however, under no obligation to enquire about or take notice of the equitable interest and if, therefore, a sole holder of the shares be a trustee, the lien will attract even in respect of his private debts to the company and will prevail over the title of the cestuique trust.

It is always open to the company, if it so chooses, to waive a lien. Besides, company's lien would be lost if it does anything showing an intention to waive the same, e. g., where it registers a transfer of shares subject to the lien.

CHAPTER V.

TRANSFER AND TRANSMISSION OF SHARES

Nature of the right to transfer Shares :

The right to transfer shares is a statutory right conferred by sec. 28, which provides that the shares or other interest (e. g. dividends) of any member shall be moveable property, transferable in the manner provided by the articles of the company. So, unless the articles provide otherwise, a shareholder has a free and unrestricted right of transfer, and the directors are compelled to register all transfers submitted to them.

The articles usually restrict the right of transfer and there is nothing to limit the restrictions which a company's articles may place on the right of transfer. Usually the directors are authorised to decline a transfer without giving any reason, or to refuse registration of a transfer of shares on which the company has a lien, or to decline registration of a transfer of partly-paid shares to a person whom they do not approve. In the case of private companies the articles restrict the right compulsorily. As observed by Lord Wrenbury, "Shares are *prima facie* transferable. But there is no law which precludes the shareholders from contracting for value that they shall each submit to any reasonable restriction which they choose to agree to. It may be for the benefit of the company that, for instance, shares shall not be transferred to rivals in the company's trade. A restriction which precludes a shareholder from transferring may be invalid, but a restriction which does no more than give right of pre-emption is invalid". As was also pointed out in the case of *Moffatt V. Tarquhar*, "This right of transfer is a right of property; and if the directors have an arbitrary power, from any fancy they choose to take up, to say there shall be no transfer, that is an annihilation of property". Where the articles give the directors a discretionary power to decline to register a transfer, they must exercise it reasonably as such power is of a fiduciary nature and must be exercised in good faith in the interest of the company. It must not, therefore be exercised corruptly, fraudulently, arbitrarily, capriciously, wantonly or for a collateral purpose. If the directors refuse registration on any wrong principle, their act can be rectified. The true legal position as regards this discretionary power of

directors to refuse or reject transfers is thus stated in the 11th edition of Buckley on companies Act at page 139.

“If the directors do give their reasons, the court will then consider whether they are legitimate or not, that is, whether the directors have proceeded on a right or wrong principle, and will over rule their decision, if their reasons are not legitimate, but not, if they are legitimate, merely because the court would not have come to the same conclusion. The court will also overrule the directors’ decision where, although they have given no reasons, it is proved that they have acted on a wrong principle or otherwise than bonafide. The principles applicable are exactly the same whether the power of rejecting transfers is absolute or limited to particular grounds”.

Mode of transfer and procedure thereto :

The mode of transfer of shares is governed by the provisions of the articles subject to the requirements of section 34. The normal mode of transfer is as below :—

(1) **TRANSFER DEED :—** Under sec. 34 (3), both the transferor and the transferee must execute the deed of transfer which must, after its due execution be delivered to the company along with the share certificate after being duly stamped in accordance with the provisions of the Indian Stamp Act. In case where the transferor transfers his entire holding, there is no difficulty, because the transferor can conveniently give his share certificate along with the transfer deed; but when he has to transfer only a part of the shares held by him, difficulty might arise. In this later case, no transferor will like to give the share certificate to the transferee; and the difficulty can be removed in any one of the following two ways :—

(I) SPLITTING OF SHARE CERTIFICATE :—

The transferor can send his certificate to the company for being split up into a number of certificates, each of a specified number of shares. This facility is provided by the companies on the payment of a nominal fee. On the receipt of the new certificates from the company, the transferor can very conveniently hand over to the transferee an appropriate share certificate representing the exact number of shares sold to him.

(II) CERTIFICATE OF TRANSFER :—

A certified transfer is one which bears a statement that the relative share certificate has been deposited with the company and

is cancelled. For this purpose, the transfer deed is sent to the company along with the share certificate for the entire holding. This share certificate is retained and cancelled by the company while the transfer deed is duly certified and a "balance ticket" is issued for the transferor. The certified transfer is, then, delivered by the transferor to the transferee, who will send the same to the company for registration after completing it.

(2) **SCRUTINY OF TRANSFER** :—After completion, the transfer deed must be lodged with the company for registration either by the transferor or by the transferee and it must also be accompanied with the prescribed registration fees and the share certificate (unless it is a certified transfer). Then, the deed etc. must carefully be scrutinised by the company secretary in order to ascertain that everything is O. K. After a proper scrutiny, when it is found in order, a receipt is usually sent to the person lodging it.

(3) **NOTICE OF LODGEMENT** :—The application for the transfer of shares may be made by the transferor or the transferee. When it is made by the transferor, and the shares to be transferred are partly paid, a notice thereof must be given by the company to the transferee under sec. 34 ; and where the transfer has been lodged by the transferee, a notice is usually sent so the transferor in order to prevent the registration of forged transfer.

(4) **DIRECTORS APPROVAL** :—The last formality in the transfer of shares is their approval by the directors at their periodical meetings, or, as is more common, by a standing Transfer Committee of the Board, whose proceedings are placed before the next meeting of directors for confirmation.

After approval by the directors, the necessary entries are made in the Register of Members. The old share certificate is cancelled and a fresh one is issued in the name of the transferee and sent to him. Under section 108, the share certificate must be issued within three months from the date of registration of the transfer.

Refusal of Transfer :

In case the company refuses to register a transfer of any shares or debentures, it must send to the transferee and the transferor notice of such refusal within two months from the date on which the instrument of transfer was lodged with the company.

If default is made in this respect, the company and every director, manager or secretary or other officer of the company who is knowingly a party to the default, shall be liable to a fine not exceeding Rs. 50/- for each day during which the default continues (sec. 34).

Forged Transfer :

A forged transfer is void and it does not give any right or title to the transferee. But if a person receiving the forged transfer has relied upon the company's certificate made out in the name of the forger, he can sue the company for damages. If the name of a true owner is removed from the register of the company on the basis of forged transfer, the company can be compelled to replace it and would be required to pay the holder all dividends that may have been declared in the interval.

Blank Transfer :

A blank transfer is one in which the transferor hands over to the transferee the share certificate with a transfer from completely blank but for the signature of the transferor. Upon the sale or mortgage of shares, it is usual for the transferor to sign and hand over to the buyer or mortgagee, what is popularly known as the blank transfer, the intention being that the buyer or mortgagee will be at liberty later on to fill up the blank and to have the transfer registered. In this case, the advantage is that the buyer is saved from the trouble of signing two forms, if he wants to resell the shares in the near future.

TRANSMISSION OF SHARES

Difference Between Transfer and Transmission :

Transfer and transmission are quite distinct from each other. The former is based upon the act of the parties ; while the later is the result of the operation of law. On the holder of shares dying, being found a lunatic or bankrupt, the company has to deal with the legal representatives of the former holder and a case of transmission of shares, as opposed to one of transfer, thus occurs. Articles of a company usually provide for such cases. The sub section 6 of sec. 34 further preserves the power of a company to register as shareholder or debenture holder any person to whom the right to any shares in or debentures of the company has been transmitted by operation of law. Thus in the case of transmission,

the formalities provided for in the case of ordinary transfer under sec. 34 of the Act are not to be observed. The term transmission, in short, means the acquisition of shares of a deceased or insolvent member through the operation of law.

Effect of Insolvency of a Shareholder :

In the case of a share holder becoming a bankrupt or insolvent, his properties vest in the Official Assignee or in the Receiver according as he is governed by the Presidency Town or the Provincial Insolvency Act, unless the articles otherwise provide. The Official Assignee or the Receiver as the case may be, can either have himself registered as the holder of the shares of the insolvent, leave them in the name of the bankrupt, transfer them without first taking them into his own name or disclaim them so as to destroy the security or affect the rights of third parties.

Procedure in the case of Death of Shareholder :

Section 35 provides that a transfer of the share or other interest of deceased member of a company made by his legal representative shall, although the legal representative is not himself a member, be as valid as if he had been a member at the time of the execution of the instrument of transfer. On the death of a member, therefore, the right to transfer the shares registered in his name is conferred by the statute on his legal representative.

CHAPTER VI

BORROWING POWERS & REGISTRATION OF MORTGAGES

Borrowing Powers of a Company :

As a rule a company has no implied power to borrow, and the authority in this connection must be found in the Memorandum and unless the object are specified in the memorandum, including the power to borrow, a company cannot usually borrow or incur loans. In the case of a trading or commercial concern and more particularly in the case of a banking concern, such a power will, however, be presumed, even if the memorandum and articles are

entirely silent, but in the case of a non-trading company, the power to borrow must be expressed in the Memorandum and Articles. If, however, the company has no express or implied authority to borrow, it may acquire it by altering the memorandum with the sanction of the Court under Sec. 12. By whatever way this power of borrowing is exercised by a company, it is always necessary to see—

(i) Whether the company possesses the requisite power to borrow ;

(ii) Whether the directors have authority to exercise that power without a resolution of the company ;

(iii) Whether there is any limit on the amount which may be raised and if so whether that limit is reached ; and

(iv) Whether the company or its directors have power to secure the repayment of money borrowed by a mortgage or charge on or any part of the assets of the company.

A company which has an express or implied power to borrow may exercise it to any extent, of course, subject to the restrictions, if any, placed by the memorandum or the articles. If a company possesses the express or implied power to borrow, it can pledge the whole of its property and undertaking as security for loans. It cannot, however, pledge its uncalled capital that has been specially earmarked as reserve capital under sec. 69 ; nor can a banking company, under sec. 277 J, create any charge upon its unpaid capital. According to section 103, a public company cannot exercise its borrowing powers until it is entitled to commence business, but it may simultaneously offer shares and debentures for public subscription before that time. Under section 87—G, a managing agent cannot exercise in respect of any company of which he is a managing agent a power to issue debentures.

If a company borrows money, it can be secured in one or more of the following ways :—

- (i) A legal mortgage of specific parts of its property ;
- (ii) An equitable mortgage by the deposit of title deeds ;
- (iii) A mortgage of chattels—moveable property ;
- (iv) Bonds ;
- (v) Promissory notes and Bills of exchange ;
- (vi) A charge on uncalled capital ;
- (vii) A floating charge ;

(viii) Debentures ;

(ix) Debenture stock, and

(x) A mortgage or charge on book debts, but not its books as they must be kept at office for inspection.

Ultra Vires Borrowing :

If a company borrows beyond its powers, or in excess of the limit fixed by the memorandum, the borrowing is ultra vires the company and void. In such a case, the contract is void and the securities become inoperative. Such an ultra vires contract cannot even be ratified and if a company ratifies it without knowledge of the fact that it was a contract entered into ultra vires, it will not be bound by the contract.

In the case of an ultra vires borrowing, the lender has no right to sue the company in respect of the loan, but he may resort to any of the following three remedies :—

(1) He has the right to interve before the money has been actually spent by the company, to follow his money and to obtain an injunction restraining the company from parting with it ; or

(2) If, however, the money has been spent away by the company, in paying off just debts owing to the creditors of the company, he may be entitled to stand in the place of the creditors and subrogate to their rights. Such subrogation will not, however, give him the same priority that the creditor, who is paid off, had to any securities for their debts held by such creditors ; or

(3) He may also bring a suit against the directors of the company on account of an implied warranty of authority. The directors are liable in such a case even if it is proved that they did not know that they were exceeding their powers. But, the directors shall not be liable if their act amounts only to a misrepresentation of law. In case the directors guarantee the repayment of loans taken by the company, and the loan is secured by an ultra vires arrangement, they are not relieved from liability as guarantors by reason of the claim being unenforceable against the company.

Where the directors borrow in excess of their powers, but the borrowing is intra vires the company, the borrowing is nevertheless irregular and securities are inoperative. The company may, however, in such a case be estopped from alleging its invalidity or the share holders may elect to ratify the act of directors.

Where the borrowing by the company itself is not ultra vires, but the directors of the company have no power to borrow,

a person lending money to the company can enforce payment, if it can be shown that the money had been bonafied applied for the purposes of the company.

DEBENTURES

What it means ?

A debenture is an acknowledgement of a debt, given under the seal of the company and containing contract for the repayment of the principal sum at a specified date and for the payment of interest at a fixed rate percent, until the principal sum is repaid and it may or may not create a charge on the assets of the company as security for the loan. Usually, it gives a charge by way of security and in most cases, it is one of the series of like debentures¹. The term debenture may be used to describe an instrument which is not called on the face of it debenture, e. g., a railway mortgage or bond. What is called a debenture may be a mere promise to repay or covenant to pay under seal or a mortgage or charge under the seal of the company².

As observed by Chitty, L. J , in *Admon V. Balania Furnace Co.*, "the term debenture itself comforts a debt—an acknowledgement of a debt—and speaking of numerous and various forms of instruments which have been called debentures without anybody being able to say the term is incorrectly used. I find that, generally, if not always, the instrument imports an obligation or covenant to pay. This obligation covenant is in most cases at the present day accompanied by some charge or security, so that there are debentures which are secured and debentures which are not secured."

The Indian Companies Act does not contain any concrete definition of the term 'debenture'. According to sec. 2 (1) (4), the term debenture includes debenture stock. A debenture stock is merely a borrowed capital consolidated into one mass for the sake of convenience. Instead of each lender having a separate bond or mortgage, he has a certificate entitling him to a certain sum, being a portion of one large loan³. Generally, it differs from a debenture in form rather than in substance, and is sometimes

1. *Palmer's Company Law*, xvi edition, Page 280.

2. *British Indian Steam Navigation Co. V. Commissioner of Inland Revenue*, 7 Q. B. D. 165 (172).

3. See *Lindley on Company Law*, Page 346.

in the nature of a permanent loan. It is generally secured by a trust deed.

DEBENTURE & DEBENTURE STOCK DISTINGUISHED

DEBENTURE	DEBENTURE STOCK
1. The term debenture denotes the description of an instrument.	1. The term debenture stock denotes a debt which is secured by an instrument.
2. Debentures are payable on a certain date expressly mentioned in the debentures.	2. Debenture stock is payable only in the event of the winding up of the company.
3. Debentures are transferable only in their entirety.	3. Debenture stock can be transferred in any proportions.

Kinds of Debentures :

Debentures are of several kinds, the following are, however, its principal varieties :—

(1) **BEARER DEBENTURES** :—It is one which is payable to the bearer thereof. They are negotiable instruments, transferable by mere delivery. The interest due is paid to the holder irrespective of his identity, and the payment of interest is usually made through coupons attached to them. They can be transferred without any notice to the company, and no stamp duty is payable on a transfer.

(2) **REGISTERED DEBENTURES** —They are payable to registered holders and recorded in the books of the company. They are not negotiable. These debentures too have interest coupons attached to them, which are negotiable and the interest is payable to the holder thereof.

(3) **NAKED DEBENTURES** :—These are debentures where no security is given to the lenders for the payment of interest and the repayment of capital. Such debentures are not, however, very common.

(4) **SECURED DEBENTURES** :—They are payable to the registered holder or to the bearer but they are issued with a charge on the undertakings and assets of the company as security. Sometimes they are also termed as Bonds or Debentures.

(5) **DEBENTURES WITH FIXED CHARGE** :—These are issued with a charge on some fixed immoveable property of the company.

(6) **DEBENTURE WITH FLOATING CHARGE** :—These are issued with a floating charge on the moveable assets of the company as security.

(7) **EQUITABLE DEBENTURES** :—They are those which are secured by deposit of title deeds of property with a memorandum in writing creating a charge on it.

(8) **LEGAL DEBENTURES** :—They are those in which the legal ownership of the property of the company is transferred by a deed to the debenture-holders as security for the loan.

(9) **REDEEMABLE DEBENTURES** :—They are those that are repayable after a stated period. Debentures issued by companies usually are redeemable.

(10) **Irredeemable Debentures or PERPETUAL Debentures** are those where either there is no fixed period for a repayment or where the repayment is made conditional on the happening of an event which may not happen for an indefinite period (sec. 126).

(11) **CONVERTIBLE DEBENTURES** :—These are those in which the holders possess an option to exchange their debentures into shares.

Fixed and Floating Charges :

Secured or Mortgage debentures can be sub-divided into two classes, viz , debentures which are secured by a fixed charge, and debentures which are secured by what is known as floating charge. A fixed charge differs from a floating charge in the sense that it attaches to specific property, and the company cannot deal with that property without the consent of the mortgagee. The following are the essential point of distinction between fixed and floating charge :—

FIXED CHARGE	FLOATING CHARGE
1. A specific or fixed charge is one which fastens on the ascertained or definite property.	1. A Floating charge is ambulator and shifting in its charge, hovering over and so to speak floating with all the

2. Here the company loses the right to dispose off the property.

property of the company, present and future.

2. It is not so here.

The principal tests as to whether the charge is a floating one or not are well laid down by their Lordships of the Privy Council as below :—

“Is it a charge upon all or certain class of assets present or future? Would the assets charged in the ordinary course of business be changed from time to time? Has the company power until such step is taken by the charges to carry on the business of the company in the ordinary way?”

Main Characteristics of a Floating :

(1) It is a charge on a class of company's assets, present and future ;

(2) that class is one which, in the ordinary course of business of the company, is changing from time to time ; and

(3) it is generally in the ordinary way in that class of assets till some step is taken by and on behalf of these interested in the charge. While the company is a going concern the mere happening of such an event is not enough to crystallize the charge but the charge or the debenture holder must, on the happening of such event, take steps with a view to realise his security. Again, it is of the essence of the floating charge that it remains dormant until the undertaking charged ceased to be a going concern or until the person in whose favour the charge is created intervenes.*

The floating charge ceases to be dormant and becomes fixed or crystallized in the following circumstances :—

(i) When the company ceases to be a going concern ;

(ii) Upon the commencement of the winding up of the company or ;

(iii) Upon the appointment of a Receiver on the request of a debenture holder who has intervened.

A floating charge is also postponed to the rights of the following persons if they act before the security crystallizes, viz.,—

(i) a landlord who distrains for rent ;

(ii) a decree-holder who attaches goods and sold them.

* Company promotion and management by A. N. Khanna, Page 125.

(iii) a creditor under absolute garnishee order.

Further, under section 129, if a Receiver is appointed in respect of debentures secured by a floating charge or possession is taken by or on behalf of such debenture-holders and the company is not in liquidation, then the Receiver or other person taking possession must pay out of the assets coming into his hands the debts which are by sec. 230 preferential in priority to the principal or interest in respect of the debentures. And, it is on account of these reasons that a floating charge is not considered as a paramount security.

Debenture Trust Deed :

When debentures are issued for public subscription, a trust deed is usually executed conveying the property of the company to trustees and declaring a trust in favour of the debenture holders, charging the property.

Its Contents are :

1. Particulars of the property charged as security.
2. Whether the charge is fixed or floating or both ?
3. Whether the company shall have power to create any mortgage having priority over the charge included in the trust deed ?
4. Provisions for the redemption of debentures.
5. Whether the debentures are registered or bearer and the manner of their transfer.
6. Power of trustees in the event of default by the company.

Under sec. 125(2), every debenture holder is entitled to have a copy of the trust deed on payment. Ordinarily, banks, lawyers, share brokers, insurance companies and investment trust act as debenture trustees. The trustees may be individuals or corporate bodies.

Advantages of such Deed Are :

- (1) It vests in the trustees, the property mortgaged, who would look after the property and the rights and interest of the debentures.
- (2) In the case of default, the trustees can take immediate steps on behalf of all the debenture-holders.
- (3) The trustees, if empowered, may enforce the security by sale of the property without the aid of the court.

(4) A legal estate is vested in the trustees, so that a subsequent legal mortgage is prevented from getting priority.

Issue of Debentures :

Debentures are issued exactly like shares. A prospectus offering the debentures is generally issued by the company. Under sec. 105, a public company cannot issue debentures until it becomes entitled to commence business. Again, a public company which does not issue a prospectus on or with reference to its formation, cannot issue debentures unless it issues and files with the Registrar a statement in lieu of prospectus before the first allotment of debentures (sec. 98 sub. sec. 1).

The power to issue debentures comes to an end only on the commencement of winding up. When the debentures are issued creating a charge, it should be expressly declared that the charge created by all the debentures of the series is to rank equally and without priority one over another. Successive series of debentures rank in order of their issue and each series is postponed to that before it, while it takes priority over all following it. All the debentures, of the first series, thus, rank 'pari passu'; which means that all the debentures of the same series are to be paid rateably so that, if there is not enough to go round, they shall all abate proportionately. On the other hand, if the words 'pari passu' are not put in, the debentures would be payable according to the date of their issue, or, if they were all issued on the same day, then according to numerical order. In case the words 'pari passu' are there, a debenture-holder who seeks to enforce his security must sue on behalf of himself and all other debenture-holders of the same series. It should also be noted that a company cannot create a new series, unless power to do so is expressly reserved.

Again, the debentures may be issued in respect of an existing debt, and may also be deposited to secure an existing debt. Similarly, debenture stock can be mortgaged or deposited as security for a loan by the company which issues it or by an ordinary holder. Further, debentures may also be issued at a discount and the principle that shares cannot be issued at a discount does not apply here. It is because the debentures do not form the capital of the company. Commission may also be paid in respect of debentures.

Re-issue of Debentures :

Under sec. 127, a company, which has redeemed any debentures is empowered to keep the debentures alive for the purpose of re-issue and to reissue them and give to the holder the same rights as if the debentures had not been previously issued and redeemed. The company is entitled to reissue the same debentures or it may issue others in their place. The power to reissue redeemed debentures cannot, however, be exercised in the following cases :—

- (i) If the articles or the conditions of issue expressly provide ; otherwise ; or
- (ii) If the debentures have been redeemed in pursuance of any obligation on the company to do so.

Where with the object of keeping alive debentures for the purposes of re-issue, they are transferred to a nominee of the company, a transfer from that nominee shall be deemed to be a reissue for the purposes of the aforesaid (sec. 127 sub sec. 2).

Where a company has deposited any of its debentures to secure advances from time to time on current account or otherwise, the debentures will not be treated as having been extinguished by reason only of the account having ceased to be in debt (sec. 127 sub sec. 3). In the case of re-issue of debentures or issue of new debentures in place of redeemed ones, the same stamp duty will have to be paid as would have been payable if the debentures were being issued for the first time (section 127 sub sec. 4. But a person who without notice or negligence takes a debenture which appears to be duly stamped (but which indeed was not duly stamped) is protected. Such person may give the debenture in evidence in any proceedings for enforcing his security without payment of the stamp duty or any penalty in respect thereof. In any such case, the company shall be liable to pay the proper stamp-duty and penalty (Proviso to sub. sec. 4 of sec. 127).

Under sec. 127 (5) (b), the power to issue debentures in place of any debenture paid off or otherwise satisfied or extinguished, reserved to a company by its debentures or securities for the same, would not be affected by sec. 127 aforesaid.

According to sec. 128, a contract with a company to take up and pay for any debentures of the company may be enforced

Transfer of debentures :

Debentures can be transferred exactly like shares. Just like transfer of shares, there must be a proper instrument of transfer duly stamped and executed by the transferor and the transferee accompanied by a scrip before it is lawful for the company to register a transfer of debentures. Section 108 further makes it obligatory for every company to have ready for delivery the certificates of debentures or of debenture stock transferred within three months after the registration thereof, unless the conditions of the issue of the debentures or debenture stock provide otherwise. The debentures payable to bearer may, however, be transferred by mere delivery.

Remedies of debenture-holders :

A debenture-holder who wishes to realise his security and get his money back, has got the following remedies :—

(1) He is entitled to sue on behalf of himself and all other debenture holders to obtain payment or to enforce his security by sale. The Court will, then, appoint a Receiver and will declare the debentures to be a charge on the assets of the company.

(2) He may also himself appoint a receiver, if the conditions of the debentures give him such powers or may ask the trustees to enter upon and take possession of the mortgaged property and sale the same if such power is reserved by the trust deed.

(3) He may app'y to the court for foreclosure of the company's right to redeem the debentures. Foreclosure may extend even to the uncalled capital of the company.

(4) He may also present petitions for the winding up of the company and the mere fact that he has obtained the appointment of a receiver does not preclude him from applying for a winding up order.

(5) He may have the property sold by the trustees if the debenture trust deed permits sale

(6) He may, at his discretion, either value his security and prove for the balance of his debt or give up the security and prove for the whole debt. He cannot, however, prove for the interest accruing due after the winding up, nor can he get interest out of his security when arriving at a balance for which he can prove in the winding up. If he owes a debt to the company, he cannot set

it off against the liability of the company, the rule being that a person who claims share of a fund must first pay up everything he owes to the fund.

Appointment of receiver :

Receiver may be appointed :—

(1) By a particular person, if the power of appointing a receiver is vested in such a person by the debentures of the debenture-trust and it is exercised in the interest of all the debenture-holders; or

(2) By the debenture holders, if the deed contains a provision to that effect and the power is exercised by the debenture holders in accordance with that provision; or

(3) By the Court, on an application made by the debenture-holders. In this case the appointment of the receiver is discretionary with the court and will be exercised whenever the security is in jeopardy, even though neither principal nor interest may be in arrears.

On the appointment of a receiver, the assets of the company get specifically charged in favour of the debenture holders and the company can no more deal with them in the ordinary course of business. If at all it is deemed essential to carry on the business, the court will either appoint the receiver as the manager or will appoint another person as manager. A receiver appointed by the court will be personally responsible to the creditors of the company, whilst he will be indemnified out of the estate. Any interference with this officer will be considered as a contempt of court. The receiver is also required to give security for the safety of assets in his hands. On a winding up, a receiver, if an agent of the company, ceases to be such, but he does not thereby become an agent of the debenture holders. In either case, he is not personally liable on contracts he makes.

Registration of receiver's appointment :

It is the duty of every person who obtains an order for the appointment of the Receiver to file a notice of the fact within 15 days of the order of appointment. Default is made punishable with a fine upto Rs. 50/- for each day so long as the default continues.

In a debenture-holder's action where there is a deficiency, the assets must be applied in the order given below :—

- (1) Costs of realization;
- (2) Costs including remuneration of receiver;
- (3) Cost, charges and expenses of debenture trust deed including, the trustees' remuneration;
- (5) Preferential creditors and;
- (6) Debentureholders.

Filing of accounts by receiver :

According to section 119 (1), every receiver of the property of a company appointed under the powers contained in any deed and who has taken possession of such property, is required to file with the registrar once in each year, an abstract in the prescribed form of his receipts and payments during the period to which the abstract relates and also to file with him, on ceasing to act as receiver, notice to that effect and the registrar must enter the notice in the register of mortgages and charges.

Where a receiver of the property has been appointed, every invoice, order for goods, or business letter issued by or on behalf of the company, or the receiver of the company, being a document on or in which the name of the company appears shall contain a statement that a receiver has been appointed (Sec. 119 sub sec 2). In case of default, the company and every director, manager, managing agent, secretary or other officers of the company and every receiver who knowingly and wilfully authorises or permits the default, shall be liable to a fine not exceeding Rs. 200/-.

Registration of mortgages :

According to section 109, the following mortgages and charges created by a company must be registered with the Registrar :—

- (1) A mortgage or charge for the purpose of securing an issue of debentures.
- (2) A mortgage or charge on the uncalled share capital of the company.
- (3) A mortgage or charge on any immovable property, wherever situated.
- (4) A mortgage or charge on any book debts of the company.
- (5) A mortgage or charge not being a pledge on any immovable property of the company except stock in-trade; and

(6) A floating charge on the undertaking or property of the company.

Section 116 (1) makes it obligatory on a company to file with the Registrar for registration the prescribed particulars of every mortgage or charge created by the company and of the issue of debentures of a series requiring registration under sec. 109. This section also provides that in default of the company discharging its obligations in respect thereof, the registration of any such mortgage or charge may be effected on the application of any interested person. Where any mortgage or charge on any property of a company required to be registered under sec. 109, has been so registered, any person acquiring such property or any part thereof, or any share or interest therein, shall be deemed to have notice of the said mortgage or charge as from the date of such registration. (Sec. 109 sub sec. 2).

Under sec. 116 (3), a company must register with the registrar the particulars of any modification of the terms or conditions or extent or operation of any mortgage or charge in much the same way as in the case of the creation of a mortgage or charge. Further, every instrument by which charge is created must be registered with the registrar within 21 days. Section 120 gives power to the court to extend time if the court is satisfied that the omission to register a charge or mortgage has been accidental or due to inadvertence or to some other sufficient cause or is not of a nature to prejudice the position of creditors or shareholders of the company, or there are other grounds which make it just and equitable to grant it relief. If the court extends the time for registration and the mortgage is registered within that time, the mortgage constitutes a valid charge at initio.

Registration of particulars in case of debentures :

Section 110 provides an alternative mode of registration of particulars in a case where a series of debentures are issued entitling the holders thereof *pari passu* to the benefits of a charge created thereby. In such a case, it shall be sufficient for the purpose of sec. 109, if they are filed with the registrar within 21 days after the execution of deed containing the charge or, if there is no such deed, after the execution of any debentures of the series, the following particulars :—

- (a) The total amount secured by the whole series.

(b) The dates of the resolution authorizing the issue of the series and the date of the covering deed, if any, by which a security is credited or defined.

(c) A general description of the property charged; and

(d) The names of the trustees, if any, for the debentureholders.

Together with the deed or a duly verified copy thereof containing the charge or if there is no such deed, one of the debentures of the series; provided where more than once issue is made of the debentures in the series, the particulars of the dates and amounts of each issue shall be filed with the registrar, but omission to do so shall not affect the validity of the debentures issued.

Further, sec. 111 requires that the particulars required to be filed for registration under secs. 109 and 110 shall also include particulars as to the amount or rate per cent of the commission, discount or allowance, paid or made, directly or indirectly, by the company to any person in consideration of his subscribing or agreeing to subscribe for any debentures of the company or procuring or agreeing to procure subscription for any such debentures. The omission to do so shall not, however, affect the validity of the debentures issued.

Effect of registration :

If any mortgage or charge has been registered, it operates as a notice of the said mortgage or charge to any person acquiring subsequent to registration. Once registration is effected and certificate is given by the registrar in respect of the document, it is a conclusive evidence that the mortgage or charge created by such document is properly registered, even though the particulars are incomplete and the entry in the register is defective (sec. 114).

Effect of non-registration :

If a mortgage or charge requiring registration is not registered, it will not confer any security on the company's property or undertaking as against the liquidator and creditors, i. e., such a mortgage or charge shall be void. The non-registration does not, however, make the transaction void as against the company so as to make the debt irrecoverable. The transaction would be void even when decrees were obtained on such unregistered mortgages prior to the winding up application.

Penalties for non-registration :

In case of default, the company and every officer thereof who is knowingly a party to it shall be liable to fine not exceeding

Rs. 500/- for each day the default continues. Where any person permits delivery of any debenture or certificate of debenture stock requiring registration, without a copy of the certificate of registration being endorsed upon it, he shall, without prejudice to any other liability, be liable on conviction to a fine not exceeding Rs 1,000/-.

Register of mortgages :

Under section 123, every company is required to keep a register of mortgages and enter therein ALL charges specifically affecting the property of the company and all floating charges on its undertaking, giving in each case a short description of the property charged, the amount of the charge and, except in the case of securities to bearer, the names of the persons entitled thereto.

Section 112 requires the Registrar to maintain a register of mortgages and charges created by each company, and enter therein the full particulars. Every member and creditor of the company is entitled to inspect this register without any fee; other persons can do so on payment of Re. 1/-. The Registrar must also keep a chronological index of mortgages and charges so registered for ready reference (sec. 113). If a company does not keep a register of mortgages and charges, there is a penalty of Rs. 500/- on every director, manager or other officer of the company who is knowingly in default.

CHAPTER VII.

CONTRACTS

Introduction :

A company being an artificial person cannot obviously function by itself. It must function only through natural persons. Therefore, having regard to the complexities of modern business and to the fact that all the shareholders of a company, which sometimes run into three or four figures, cannot be expected to have a direct say in the affairs of the company, regulation 71 of Table A, which compulsorily applies to all companies, vests the management of the business of a company in its directors. Most of the companies in

India also appoint managing agents, in addition to directors, for the management of their affairs. And, these are the directors and managing agents who represent the company in dealings with third parties.

Common seal :

Common seal acts as the official signature of the company. According to section 73, every company is required to have a common seal upon which the company's registered name must be engraved in legible characters. A rubber stamp cannot serve the purpose of a common seal. The company may, by writing under its common seal, give any person a general or particular power of attorney to act on its behalf and execute deed anywhere on its behalf, and such act or deed will be binding on the company.

Its use :

Invariably, the articles contain provisions governing its use. According to regulation 76 of Table A, the seal shall not be affixed to any instrument except by the authority of a resolution of the directors, and in the presence of at least two directors and of the secretary or such other person as the directors may appoint for the purpose, who will sign every instrument to which seal is so affixed in their presence. Thus, every document does not require the seal of the company. Common seal of the company is required to be affixed only on those documents for which sealing is made compulsory, such as share certificates, share warrants, debentures, and other important contracts. Other documents made on behalf of the company are simply signed by the directors and not sealed.

Official seal :

Where the objects of the company require the transaction of the business outside India, it may, if authorised by its articles, have an official seal for use abroad. It is usually a facsimile of the common seal of the company with the addition of the name of the place where the seal is to be employed. A company having an official seal may, by writing under its common seal, authorise its attorney in that place to affix the same to any document to which the company is a party (sec. 91 sub sec. 1).

General rules with regard to contracts :

The following general rules must be kept in view in contracts with a company .—

(1) Any contract made by a company before the date on which it is entitled to commence business, shall be provisional only

and shall not be binding on the company until that date and shall become binding on that date.

(2) The contractual capacity of a company is restricted by its memorandum. A contract entered into by the company shall be void, if it is ultra vires (i. e., beyond the powers prescribed by the the memorandum). Such an ultra vires contract cannot even be ratified and if a company ratifies it without knowledge of the fact that it was a contract entered into ultra vires, it will not be bound by the contract.

(3) If a contract is ultra vires the company but is ultra vires the directors, as being in excess of their authority, it shall be invalid, but it may be ratified by the shareholders. If the company does not ratify it, it shall not be liable unless the case falls within the rule laid down in *Royal British Bank V. Turquand*. This rule provides that although a person who deals with a company is bound to read the Act and registered documents in order to ascertain that the contract is not inconsistent with them yet he is not bound to enquire into the regularity of the company's internal proceedings.

(4) A contract entered into on behalf of a company before its incorporation by its promoters cannot be ratified by a company after its incorporation, though a company may, after its incorporation, enter into a new contract embodying the terms of the old contract.

Form of contracts :

As regards the form of contracts the following observations of Mr. Boville, C. J. in an English case are worth noting :—

“Originally all contracts by corporations were required to be under seal. From time to time certain exceptions were introduced but these for a long time had reference only to matters of trifling importance and frequent occurrence, such as hiring of servant and the like. But, in progress of time as new descriptions of corporations came into existence, the courts came to consider whether these exceptions ought not to be extended in the case of corporations created for trading and other purposes. the exceptions created by recent cases are now too firmly established to be questioned by earlier decisions on the subject. These exceptions apply to contracts by trading corporations.”.

In another case it has been held by Wrightman, that whenever a contract is made with relation to the purposes of the corporation

it may, if the corporation be a trading one, be enforced, though not under seal.

Sections 88 to 91 D deal with the form of contracts. According to section 88, contracts on behalf of a company can be made by any person acting under its authority, express or implied, exactly in the manner as they are required by law to be entered into between natural born persons either in writing or orally. All such contracts shall be effectual in law and shall bind the company and its successors and all other parties thereto, their heirs, or legal representatives as the case may be. It should be noted here that once the right of a party dealing with a company have become fixed by a contract, the company cannot, by a resolution subsequently passed by it, alter those rights.

Under section 89, two conditions must be fulfilled before a B/E, P/N or a hundi can be binding on the company :—

(1) The B/E, P/N or hundi must have been made, drawn, accepted or endorsed in the name of the company or by or on behalf of the company; and

(2) It must be so made, drawn, accepted or endorsed by a person acting under its authority express or implied. It is of utmost importance that the name of the company should be clearly stated on the document so that the responsibility is made plain and can be instantly recognised as the document passes from hand to hand.

The liability of a company with regard to such instrument depends upon the nature of their construction. The company shall be liable, if on the true construction, the bill, note or hundi seems to be that of the company, otherwise not. For example if a P/N is accepted by X "For and on behalf of A & Co. Ltd". A & Co. Ltd. shall be liable and not Mr. X. But, on the other hand, if the construction of the instrument is like this—"X, Managing agents of A & B Co. Ltd". The company A & B Co. Ltd. shall not be liable, as its responsibility is not clear. Similarly, where a directors executes a bill or the hundi merely describing himself as the director of a company, the company cannot be held liable; but the liability of the director is not excluded*.

*Damodar V. Ramnath (1932, 34 B. L. R. 1327.

Execution of deeds :

Under sec. 90, a company may, by writing under its common seal (as already defined) empower any person, either generally or in respect of any specified matters, as its attorney, to execute deeds on its behalf in any place within India (and it may have an official seal for use abroad); and every deed signed by such attorney shall bind the company and have the same effect as if it were under its common seal.

Contract with Directors :

A director stands in a fiduciary relation with a company and therefore cannot enter into a contract with the company of which he is a director. Secondly, he is also prohibited from having an interest, direct or indirect, in any contract entered into by or on behalf of the company of which he is a director. Sections 91-A to 91-C, however, permit a director to make such contracts on certain conditions. Section 91-A provides that every director who is directly or indirectly concerned or interested in any contract or arrangement entered into by or behalf of the company, must disclose the nature of the interest at the meeting of the directors at which such contract is executed. If he acquires interest subsequently, he must disclose it at the first meeting thereafter. Further, a director must not vote at a Board meeting on such a contract; and if he does vote, his vote will not be counted, and he shall also be liable to a fine upto Rs. 1,000/- in addition to his liability to account for secret profit (sec. 91-B). The reason of these provisions, as pointed out by Lord Cairns in *Parker V Mackenna*, is that no man acting as an agent can be allowed to put himself in a position to which his interest and duty will be in conflict. The company is entitled to the collective wisdom of its directors, and if any of such directors is interested in a contract, the company loses the benefit of the director's unbiassed judgement. The duty to disclose is based more or less on the principle that where there is a conflict between duty and interest, an agent must disclose any undertaking likely to result in any gain to him, arrived at between the servant or agent and a third person who enters into a contract with the master or principal, otherwise such a secret bargain, being a fraud on the master or principal, will entitle the latter to rescind the contract with such third person.*

It is not necessary to make a formal disclosure, where, however, the nature of the interest is known to all the directors.

*Company and Promotion and management by A. N. Khanna (Page 152).

Non-disclosure in other cases will make the director liable to a fine upto Rs. 100/-

Contracts of Appointment of Manager or Managing Agent :

Section 91-C provides that where a company enters into a contract for the appointment of managing agent of the company and some director is directly or indirectly interested in that contract, the company must send within 21 days of such a contract of appointment, an abstract of the terms of such contract together with a memorandum clearly indicating the nature of the interest of the director in the contract to every member, and keep a copy thereof at the registered office of the company which shall be open to inspection by any member. This procedure is equally applicable to any variations made in such contracts. The default in complying with these requirements makes the company liable to a fine upto Rs. 1,000/- and every officer of the company who knowingly or wilfully authorises or permits the default shall be liable to the like penalty.

Company as Undisclosed Principal :

Where a manager or other agent of a company (other than a private company) enters into a contract on behalf of the company, without disclosing its name, he shall at the time of making a contract, make a memorandum, in writing containing the terms of the contract and deliver the same to the company forthwith to be placed before the next meeting of the directors and also deliver copies of the memorandum to them. The default in complying with these requirements makes the contract at the option of the company, void as against the company and further makes the Manager and other officer guilty of default liable to a fine not exceeding Rs. 200 - (sec. 91-D). The object of this provision is to put a stop to the practice by agents or managers of entering into contracts in their own names for and on behalf of the company without disclosing to the other parties the names of the company.

CHAPTER VIII

LAW RELATING TO DIRECTORS

The law relating to directors of a company is contained in sections 83-A to 87 and regulations 71 and 78—82 of Table A, and is discussed in the following paragraphs.

Definition of Director :

It is really strange that the Indian Companies Act does not precisely define the term 'Director'. Sec. 2(5) simply states that "director includes any person occupying the position of a director, by whatever name called." So, the function is everything, name matters nothing. As a matter of fact, a company has no person and so it cannot act in its own person ; it must act through its agents, and usually those persons through whom it acts are known as what we call, directors. Collectively the directors are designated by the term "Board" ; in some cases, however, they are described as "Governing Body" or "Committee of the Management."

Number of Directors :

According to section 83-A, every company (other than a private company, not being a subsidiary company of a public company) MUST have at least THREE directors. From this section, it appears that private companies need not have any directors. But, as regulation 71 of Table A, which compulsorily apply to ALL companies, provides that "The business of the company—private as well as public—shall be managed by the Directors," it is obvious that even private companies too must have directors. They may not have necessarily three directors. If a private company does not appoint directors as such, but leaves the management of its business in the hands of shareholders themselves they would be deemed to be directors in the eye of law.

Where the articles unequivocally provide for the maximum and minimum number, the shareholders cannot vary that number in general meeting without first altering the articles by a special resolution. But, if power is reserved in the article for the shareholders in general meeting to vary the number of directors, they can alter the number of such director in general meeting (of course, subject to the minima prescribed by sec. 83-A), without an alteration in the articles concerned.

Position of directors :

The precise position of directors is hard to define. The Act is silent on this point and does not define their status. In the words of Lord Selbourne, "the directors are the mere trustees or agents of the company—trustees of the company's money and property; and agents in the transaction which they enter into on behalf of the company." Whatever the name, their true position is that "they are commercial men managing a trading concern for the benefit of themselves and of all the shareholders in it." Lord Cranworth in *Aberdeen Railway Co. V. Blackis* described them as a body to whom is delegated the duty of managing the general affairs of the company, observing further that a corporate body can only act by agents and it is, of course, the duty of those agents so to act as best to promote the interest of the corporation whose affairs they are conducting and as such they have duties to discharge, of a fiduciary nature, towards their principal.**

Duties of Directors :

The duties of directors are regulated by the company's articles and depend upon the nature and size of the business of each company. Although it is difficult to describe and enumerate all the duties; yet their principal duties may be mentioned as follows :—

(1) Duty of Directors as Agents of the Company :

Directors are the agents of the company with the duty to carry on the whole of its business subject to restrictions imposed by the Act and/or the articles. The general law of agency governs to an appreciable extent the relationship between the company and its directors. They stand in a fiduciary relation to the company in the sense that if they make any unfair advantage on account of their position, they are liable to account for the resulting profit. Being fiduciary donees of their powers, they are bound to exercise them for the benefit of the members generally and not for the benefit of themselves or for the benefit of any particular member. It means that, they must approve transfers, make calls, issue and allot shares, declare dividends or make investments in the interests of the company as a whole and not in the interest of any particular individual or individuals. Further, a director is disqualified from contracting with the company either on his own behalf or any

* Extracted from "Company Promotion & Management by A. N. Khanna, Page 155.

company or firm, in which he is interested as shareholder or director without the sanction of the company in general meeting, unless the article authorise him to do so.

(2) Duty Of Directors As Trustees :

Directors are the trustees of company's money and property and are bound to exercise the trust with fidelity and reasonable diligence. Courtney Terrel, C. J. in one of his judgements, observes as below :— 'This is not a case in which the contract is entered into between two independent persons ; it is in the nature of a contract between the trustee and his cestui que trust. The trustee, by discharging a small portion of the cestui que trust indebtedness puts himself in the position of a secured creditor as against the unsecured creditor, and the Government, therefore, prevents the company from paying its creditor equitably. . . . It is not right that the director of an insolvent company about to go into liquidation should be allowed the privileged position of a secured creditor by merely discharging a small portion of the company's indebtedness.

As trustees, it is the duty of each director to see that the company's money is, from time to time, in the proper state of investment. In discharging these duties, "a director must", in the words of 'Romer. J*', "act honestly, must exercise such degree of skill and diligence as would amount to the reasonable care which an ordinary man might be expected to take in the circumstances on his own behalf. He need not exhibit in the performance of duties a greater degree of skill than may reasonably be expected from a person of his knowledge and experience, in other words, he is not liable for mere errors of judgement ; he is not bound to give continuous attention to the affairs of his company : his duties are of an intermittent nature to be performed at periodical board meetings and at meetings of any committee to which he is appointed and, though not bound to attend all such meetings, he ought to attend them when reasonably able to do so. . . . A director may delegate duties, but he cannot shirk responsibility by leaving everything to others. A director should before he signs a cheque or parts with a cheque signed by him satisfy himself that a resolution has been passed by the Board or Committee of the Board authorising the signature on the cheque ; and where the cheque

* In re Equitable Insurance Co. (1825) 1 Ch. 407.

has to be signed between meetings he should get confirmation of the Board subsequently."

(3) Other Statutory & Miscellaneous Duties :

(I) DUTY WITH REGARD TO BOOKS OF A/c—Under sec. 130 (1), it is the duty of the directors to see that the company keeps proper books of accounts with respect to :—(a) all sums of money received and spent by the company, (b) all sales and purchases of the goods by the company, and (c) the assets and liabilities of the company. The default in this respect is punishable with a fine upto Rs. 1,000/-

(II) DUTY WITH REGARD TO ANNUAL GATHERING—Under sec. 76 of the Act, it is the duty of the directors to call annual general meeting of the company within 18 months from the date of incorporation and thereafter once in every year.

(III) DUTY WITH REGARD TO FINAL A/cs :—The directors of every company are required under sec. 131 (1) to lay before a general meeting of members in each calendar year a Balance Sheet and Profit and Loss a/c. The first accounts must be presented at some date not later than 18 months after the incorporation of the company and the subsequent accounts must be presented atleast once in each calendar year. The directors should also make out and attach to every Balance Sheet a report with respect to the state of company's affairs and/or the amount, if any, which they propose to carry to reserves along with their recommendations for dividend (sec. 131-A). The directors are, however, not responsible for declaring a dividend unwisely. A director must not pay dividend out of capital, and if he does so, he shall be liable, but the onus of proving that they have done so, lies upon the person who alleges it. Declaration and distribution of dividend by blindly trusting a dishonest manager, when there are no profits to the company, amounts practically to a distribution of capital and makes the directors liable.

(IV) DUTY WITH REGARD TO ALLOTMENT—Allotment of shares is a very important duty of directors and they must in this connection comply with the requirements of sec. 101 and 104 relating respectively to restrictions and return as to allotment. They should allot shares on the best terms available and in doing so they must act bonafide in good faith in the best interests of the company ; and if the allotment is irregular or is

for ulterior object, e. g., for increasing voting powers with a view to obtain the control of the company, or for the purpose of defeating the wishes of the existing majority etc ; the directors are guilty of breach of trust.

(V) DUTY AS TO ENFORCEMENT OF CALLS—It is the duty of the directors to take all steps necessary for enforcing payment of calls and they would be guilty of breach of duty if they do not do so.

(VI) DUTY AS TO FILING ANNUAL LIST OF MEMBERS AND SUMMARY—Under sec. 32, it is the duty of the directors to forward the annual list of members and summary to the registrar. Failure to do so means a *prima facie* breach of duty for which all the directors shall be liable.

(VII) DUTY TO CALL EXTRA-ORDINARY GENERAL MEETING ON REQUISITION—Under sec. 78 (1), it is the duty of the directors to call an extra-ordinary general meeting on the requisition of shareholders of not less than 1/10 of the issued share capital of the company, upon which all calls and other sum have been paid.

(VIII) DUTY AT SHAREHOLDERS' MEETINGS—Directors must give information of all relevant facts to be discussed at the shareholders' meeting. Further, it is their duty to forward to the members of the company any reason which they think justified, the policy which the company, with their assistance, has adopted and to say to the members, if they think so in good faith, that it is the best policy and are bound to do so, if it is attacked by a member.

(IX) DUTY AS TO STATUTORY MEETING—Under sec. 77 (2) it is the duty of the directors to send a statutory report to each shareholder at least 21 days prior to the holding of the statutory meeting, and under sub sec. 3 of the aforesaid section, such report must also be certified by not less than two directors of the company or by the chairman of the directors, if authorised in this behalf by the directors. Under sub sec. 5, they are required to send copies of the report to the registrar for registration as soon as copies thereof are sent to the members, Sub sec. 6 further imposes an obligation to cause a list of members showing certain particulars enumerated therein to be produced at the commencement of the

meeting and to keep that list at the meeting available for inspection of the shareholders during the continuance of the meeting.

(X) **DUTY TO DISCLOSE INTEREST**—Under sec. 91—A, it is the duty of every director who is directly or indirectly concerned or interested in any contract entered into by or on behalf of the company, to disclose the nature of his interest at the meeting of the directors at which that contract is to be determined.

Powers of directors :

The powers of directors are generally given in the articles. However, the compulsory regulation 71 of Table A lays down that the business of a company shall be managed by its directors. This regulation expressly delegates to the directors the power to do everything that the company can do except where the authority of a general meeting of the company is expressly prescribed by the Act and the articles of the company. The directors, being themselves the delegator of the shareholders cannot delegate their authority to anybody also and the maxim “*Delegatus non potest delegare*”—will apply in this connection. If however, the articles permit, they may delegate some of their powers to managing agents, of course, subject to restrictions imposed by the Act. Further, the shareholders may enlarge the powers of the directors so as to enable them to do anything that the company can do, and if the directors do anything in excess of their powers, the shareholders may ratify such act, if it is within the powers of the company. Some of the principal powers of directors, as already pointed out, consist of allotment of shares, making calls, forfeiture of shares, rejection or approval of transfers, making contracts, recommend dividends, incur capital expenditure etc. etc.

Directors' powers cannot be interfered with by shareholders :

A company is an entity distinct alike from its members and shareholders. Some of its powers may, according to its articles, be exercised by directors, while certain others may be reserved for the members in general meeting. It is a first and elementary principle of Company Law that where the specific powers are vested in the directors, they reside with them *exclusively* and cannot be exercised or interfered with even by the majority of the shareholders as such. If the shareholders are dissatisfied with what the directors do, their only remedy is to remove them if they can, in the manner provided by the articles. The law on this point has been correctly

summarised by Geer, L. J., in *John Shaw and sons Ltd. V. Shaw* as below :—

“..... If the powers of management are vested in directors, they and they alone can exercise these powers. The only way in which the general body of the shareholders can control the exercise of the powers vested by the articles in the directors is, by altering their articles, or, if opportunity arises under the articles, by refusing to re-elect the directors of whose action they disapprove. They cannot themselves usurp the powers which by the articles are vested in the directors any more than the directors can usurp the powers vested by the articles in the general body of shareholders”.

Interference of courts with the directors' powers :

As a general rule, the courts seldom interfere with the internal management of a company. The courts intervene only when the directors are likely to abuse their powers. The following are some of the cases in which the courts have interfered, viz :—

(1) **WHERE SHARES ARE NOT ISSUED BONAFIDE—**Where shares were not issued bonafide for the general benefit of the company, but were issued with the object of controlling the majority of shares, and obtaining the necessary statutory majority for passing a special resolution, it was held that the directors be restrained from holding the meeting at which the votes of the new shareholders were to have been used¹.

(2) **WHERE POWER TO FORFEIT SHARES IS ABUSED—**The Court has interfered to prevent the abuse of power of forfeiture where such power was not exercised bonafide by the directors in the interests of the company, but was exercised merely to enable a shareholder to escape liability².

(3) **WHERE RESOLUTIONS ARE INCONSISTENT WITH ARTICLES—**In *Fuir and Axrens Ltd V. Salmon*, where the resolution of the directors, though confirmed in general meeting by a majority of shareholders, were inconsistent with the provisions of the articles, it was held that the company be restrained from acting upon them.

(4) **WHERE THE POWER OF MAKING CALLS IS ABUSED—**In *Alexander, Automobile Telephone Co.* where the

1. *Punt. V. Symmons & Co. Ltd.*, (1902) 2 Ch. 506 following *Fraser V. Whalley* (1864) 24 and M 10.

2. *Richmonds' case* and *Painters' case* (1858) 4 K. and J, 305.

directors abused the power of making calls, it was held that they committed a breach of duty even though in so doing they acted without fraud.

(5) **WHERE THEY HAVE REFUSED TO REGISTER TRANSFER OF SHARES**—Where the directors, who had power to refuse to register transfer of shares, have exercised that power capriciously or unfairly, the Court has jurisdiction to interfere. But, if they have bonafide considered the questions at a meeting of the board and have acted reasonably, the Court would not interfere with their discretion, and they are not bound to disclose their reasons for refusing a transfer*.

Ultra vires acts of director :

The law with regard to ultra vires acts of directors is nicely summarised in the following words by Kanhaiya Lal, J., in *Ram Bavan V. Mufassil Bank Ltd.* :—

“The authority of the directors is defined by the Memorandum and the Articles of Association and they have no power to go beyond the authority given to them, or to undertake any transaction outside the scope of the business of the company. They have power to carry on the business of the company in accord with the provisions therein contained, and if they do anything beyond the scope of the business of the company, their act is ultra vires and void, as the company would not be bound by any act done by directors for objects, which the company has no power to entertain. But not only do the acts of the directors bind the company, when done within the scope of their authority, but also where the acts of the directors, however irregular, belong to a class of acts, which is authorised by the constitution of the company. A company is bound by its dealings with strangers who act bonafide with the company ; for says Grant, “a company is liable for all acts done by its directors, even though unauthorised by it, provided such acts are within the apparent authority of the directors and not ultra vires the company”.

In certain cases however, the directors have been held personally liable for such ultra vires acts, on the ground of the breach of warranty of authority.

Rights of directors :

As a matter of fact there is no hard and fast line between the powers and rights of directors, and in most cases their powers and

* *Gresham Life Assurance society Exparte Perny* (1872) L. R. 8 Ch. A 446.

rights overlap each other. However, some of their rights may be enumerated as follows :—

(1) Under regulation 71 of Table A, they have a right to manage the affairs of the company.

(2) The directors also possess a right to attend the meetings of the board and are entitled to receive due notice thereof.

(3) Under sec. 130 (2), they have a right to inspect the books of account of the company.

(4) The directors have a right to recommend the amount which they decide should be paid by way of dividend.

(5) Last, but not the least, the directors being both agents of and trustees for the company, are entitled to be indemnified by the company against all losses and expense properly sustained and incurred by them in due performance of their office.

Appointment of directors :

The law relating to the appointment of directors may briefly be summarised as follows :—

1. **FIRST DIRECTORS**—The directors of a company are usually selected by the promoters and are named in the Articles. But, their appointment shall not be valid unless each of the proposed directors, before the registration of the articles or the publication of the prospectus has—

(a) Signed and delivered to the Registrar a consent to act as director; and

(b) Either (i) signed the memorandum for his qualification shares, or (ii) taken up and paid for them, or (iii) signed a contract to take them from the company and pay for them, or (iv) signed a declaration that a number of shares sufficient to qualify him are registered in his name (sec. 84 (1)). This provision does not apply to a private company, or a private company afterwards converted into a public company (sec. 84 (3)).

2. **SUBSEQUENT DIRECTORS**—All the first directors of a company compulsorily go out of office at the first ordinary annual general meeting, and are, then, appointed by the members. As regards these subsequent appointments, the managing agents may, under sec. 87—I, appoint upto 1/3 of the total number of directors. Then, one or two seats are reserved for appointment by special

interests, such as Government, states, preference shareholders, debentureholders, municipal or district boards, etc., leaving only a few directors to be appointed by shareholders in general meeting.

3. **ROTATION OF DIRECTORS**—According to section 83—B (2), atleast $\frac{2}{3}$ of the whole number of directors of a public company formed after 15 January, 1937, shall be person whose period of office is liable to determination at any time by retirement of directors in rotation. The provisions as to rotation of directors are contained in regulations 78 to 82 of Table A, which are compulsory in view of sec. 17 (2). These regulations in short provide as follows :—

(i) At the first ordinary meeting of the company, the whole of the directors shall retire from office, while at the ordinary meeting in every subsequent year $\frac{1}{3}$ of the directors for the time being or the number nearest to $\frac{1}{3}$ (if their number is not three or a multiple of three) must retire from office (Regulation 78).

(ii) The directors who have been longest in the office since their last election must retire first, but as between persons who became directors on the same day, it must be determined by lot as to who should retire first, unless they otherwise agree among themselves (Regulation 79).

(iii) A retiring director is eligible for re-election (Regulation 80).

(iv) The company may fill up the vacated office by electing a person thereto at the very general meeting at which a director retires by rotation (Regulation 81).

(v) If at any meeting at which an election of directors ought to take place, the place of the vacating directors are not filled up, the meeting shall stand adjourned till the same day in the next week at the same time and place, and if at the adjourned meeting the places of the vacating directors are not filled up, the vacating directors or such of them as had not their places filled up shall be deemed to have been re-elected at the adjourned meeting (Regulation 82).

The ostensible object of sec. 83—B (2) was to prescribe that $\frac{2}{3}$ of the directors of any company shall retire by rotation and be reappointable only by election by the shareholders. But, as pointed out by Messrs. Sarkar and Sen in their famous commentary on the Indian Companies Act, the object for which this sub section

was introduced has failed, because of the absence of a further provision in the said sub section or in fact any where in the Act that the persons to be appointed as directors in place of the retiring ones must be elected by the shareholders

4. **FILLING UP OF A CASUAL VACANCY**—The casual vacancy mean any vacancy arising otherwise then by retirement in usual course and includes vacancy caused by death resignation or bankruptcy. Usually the articles provide for filling up of any casual vacancy in the Board of Directors. In default of and subject to any regulations in the articles, however, any casual vacancy may be filled up by the directors, although the director so appointed will hold office only up to the time, when his predecessor would have retired, (if he were subject to retirement by rotation).

5. **THE CHAIRMAN OF THE BOARD OF DIRECTORS**—as well as of the company is appointed by the managing agents from amongst their own nominees.

Additional directors :

Regulation 85 of Table A authorises directors in their discretion, to appoint additional directors from time to time. This power, however, can be exercised only so long as the maximum number of directors as fixed by the articles is not exceeded.

Who may be appointed director ?

Generally the articles contain provisions as to who can be appointed as a director. Such person may be a company, because there is nothing to prevent a limited company from being a director. To have qualification shares, is not a legal necessity for directors ; it is not obligatory for a company to have a provision in its articles in this respect. Where there is no such provision, even a person holding no share of the company may be appointed a director. The Act simply states that if qualification shares are required by the articles, they must be acquired by the person acting as a director, within two months after his appointment or such shorter time as may be fixed by the articles (sec. 85 (1)). If the shares are not so obtained, the office becomes vacant and the person acting as director renders himself to a fine. Section 86 provides that the acts of director will be valid not withstanding any defect

that may afterwards be discovered in his appointment or qualification. The object of this provision is to make the honest act of de facto director as good as the honest acts of the de jure director.

The first director must take their qualification shares from the company direct, but subsequent directors are not bound to do so, and may acquire them by transfer, transmission or in any other manner. Shares or stock represented by share warrants cannot form part of any share qualification required by the articles (sec. 46). According to section 93, the share qualification of directors if any, is to be stated in any prospectus issued within one year of the company being entitled to commence business. According to section 103, (1) (b), a company cannot commence its business until the directors have paid for their qualification shares in cash in the same proportion as payable on application and allotment of the shares by other members of the public.

Kinds of Directors :

Directors are known by different designations according to the mode of their appointment, e g. *Ex-Officio* director is one who is usually appointed by the managing agents. *Debenture* director is one who is appointed by the debentureholders. Those appointed by other interests are known as *Special* directors. Directors appointed by shareholders are known as ordinary or *Members'* directors. Directors appointed by the policyholders in an insurance company are known as *Policyholders'* directors.

Disabilities of directors :

In order to make the position of directors more compatible with the interests of the company, the Amendment Act, 1936 has introduced a number of disabilities, which are as follows :—

(1) Under sec. 86-A an undischarged insolvent cannot act as a director, and if he so acts, he is liable to imprisonment not exceeding two years or to a fine not exceeding Rs. 1000/- or to both.

(2) Under sec. 86-B, a director is prohibited from assigning his office to any other person without the sanction of a special resolution of the company. It is, however, possible for the director to appoint an alternate or substitute director to act for him during an absence of not less than 3 months from the district in which board meetings are usually held provided that such alternate or substitute is appointed with the approval of the board of directors

and that he vacates office if and when the appointer returns to the district.

(3) A director cannot be relieved of any legal liabilities by a provision in the articles. Sec. 86-C in fact prohibits a director from contracting out of his legal responsibilities.

(4) Section 86-D prohibits loans being made by a public company to any director of the company or to a firm of which such a director is a partner or to a private company of which such a director is a member or director. But, there is nothing to prevent a nominee of a director from receiving a loan from the company for the benefit of the director and negotiating a pro-note in his own name. If anything in contravention of this provision is done, every person party to such contravention shall be liable to a fine upto Rs. 500/-, and if the debt is not repaid, all will be jointly and severally liable for the amount unpaid. This section does not apply to a banking or a private company.

(5) Under sec. 86-E, a director or a firm of which such director is a partner or a private company of which such director, is a director, is precluded, without the consent of the company in general meeting, from holding an office of profit under the company except that of managing director, manager, legal or technical adviser, banker or managing agent. This, however, does not apply to a director appointed to an office of profit before 15th Jan; 1937. Further, the office of managing agent does not fall under this disability provided by sec. 86-E.

(6) Under sec. 86- without the consent of the directors, a director of the company, or the firm of which he is a partner or any other partner of such firm, or the private company of which he is a member or a director, cannot enter into any trading contract with the company, because it involves a conflict between duty and interest. Under sec. 91-A, of course, an interested director is required to disclose his interest at the meeting of directors, and under sec. 91-B, he cannot vote on the contract in which he is interested nor is he included in the quorum.

(7) Under sec. 87-G, a company may by means of an extraordinary resolution remove any director whose period of office is liable to determination at any time by retirement of directors in rotation, and may by ordinary resolution appoint another person in his stead.

(8) Under sec. 86-H, the directors of a public company or of a subsidiary company of a public company cannot except with the consent of the company in general meeting, sell or dispose of the undertaking of the company, or remit any debt due by a director, and

(9) Last, but not the least, a director also cannot delegate his powers, unless the articles expressly give him power to do so.

Vacation of office of director :

The office of a director will be ipso facto vacated, if he—

1. fails to obtain his qualification shares, if any, within 2 months after his appointment or such shorter time as may be fixed by the articles, or if he, at any time thereafter ceases to hold the share qualification, if any, necessary for his appointment ;

2. is found to be of unsound mind by Court ;

3. is declared as an insolvent ;

4. fails to pay calls made on him in respect of shares held by him within 6 months from the date of such calls being made ;

5. without the sanction of the company in general meeting, accepts or holds any office of profit under the company, other than that of a managing director, or manager, or legal or technical adviser or a banker ;

6. absent himself from 3 consecutive meetings of the directors for a continuous period of 3 months. Whichever is longer without leave of absence from the Board ;

7. Accepts a loan or guarantee from the company in contravention of sec. 86-D ; or

8. enters into any contract for sale, purchase or supply of goods and material with the company, except with the consent of the directors, in contravention of sec. 86-F.

In addition to the above mentioned contingencies, the company may provide by its articles that the office of a director shall be vacated on grounds other than those specified above. (Section 86-I).

How do the directors act ?

Usually the directors of a company direct the affairs by decisions of the majority. In certain cases, of course, a statutory majority is required, e. g., (i) the managing agents of a company cannot enter into any trading contracts with it without the consent

of 3/4 of the directors present at board meetings and entitled to vote on the resolution ; or (ii) the managing agents of a company cannot invest the funds of one company in the shares and debentures of another company under their management, unless the purchase has been previously approved by a unanimous decision of the board of directors of the purchasing company.

Removal and resignation :

Under sec. 86-G, a company, may by means of an extraordinary resolution remove any director whose period of office is subject to determination at any time by retirement of directors in rotation before the expiration of his period of office and may also appoint by ordinary resolution another person in his place. The grounds for the removal of a director not subject to retirement by rotation may be provided by the articles.

A director can, subject to the articles of association, at any time resign his office by a notice in writing, but he cannot withdraw his resignation without the consent of the company. A resignation once made is irrevocable.

Remuneration of directors :

Prima facie directors of a company cannot claim remuneration, and consequently they are not entitled as of right to a remuneration, whether upon a quantum merit or otherwise. Therefore, unless the articles provide (and the articles usually provide) the directors are not entitled to any remuneration. If in the absence of a provision in the articles, any remuneration is paid to the directors, that shall be in the nature of a gratuity which can be sanctioned by only the company in general meeting. Usually the articles fix the definite amount of fees or salary payable to each director, or else, as is more, they provide that the remuneration of a director shall be such amount not exceeding the sum named as the directors may from time to time determine. The remuneration of directors may consist of fees or salary, a percentage of profits, special remuneration for some extra work done on behalf of the company, and travelling expenses. The remuneration payable to directors is to be disclosed in the prospectus of a new company and also in the P & L. a/c of all companies.

The remuneration of a director ceases from the moment when he ought to have vacated his office. The remuneration of directors can be paid out of capital, if there are no profits. If a director

is a trustee of his qualification shares, he may retain his remuneration for himself. Further, it is competent for a company under properly framed articles to fix different remunerations for different directors.

New restrictions :—

Under section 86—J, (inserted by the Indian Companies Amendment Act, 1951) without the approval of the Central Government, no amendment can be made in the articles of association of a public company, nor can any variation be effected in any agreement which relates to the appointment of a managing director or appointment or election of a director not able to retire by rotation. Moreover, any increase in the number of directors or their remunerations cannot be without the approval of the Central Government. Further, the articles also cannot be amended to increase the number of directors without the approval of the Central Government, nor can a new managing director be appointed after 21st. July, 1951 with such approval. The reappointment of a managing director who is holding office as such on that day or thereafter is also prohibited without the approval of the Central Government,

Further, a managing agent, managing director or any other director is also authorised under this new section to complain to the Central Government that a change in the ownership of the shares, or in the board of directors is likely, if allowed, to affect prejudicially the affairs of the company. On the merits of the complaint, the Central Government may direct that no resolution passed or action taken to effect a change in the board of directors after the date of the complaint shall have effect unless confirmed by the Central Government.

Liability of directors :

The directors of a company may incur liability in various ways as follows :—

1. In the first place, the liabilities of directors to the outsiders as to contracts are governed by the ordinary law of the principal and agent. The directors as agents of the company, are not therefore, liable to outsiders for the acts or defaults of the company. They may become liable to pay damages to outsiders for contracts only when they exceed their authority or when they contract in their own name.

2 Secondly, the directors may become personally liable for ultra vires acts :—

(i) On a breach of an implied warranty of authority where they enter into contracts ultra vires the company.

(ii) On ultra vires exercise of their powers viz, (a) wrongful acceptance of surrender of shares, (b) recommending dividends without making good the loss of circulating capital, (c) misapplication of company's funds, (d) payment of wrongful or fraudulent declaration of dividends out of capital etc. etc.

3. Thirdly, the directors may become liable to pay damages for untrue statements in the prospectus or statement in lieu of prospectus.

4. A director who habitually abstains from Board meetings may become liable for the acts of his co-directors.

5. Directors are also liable to vacate office, to retire in rotation, to be removed from office and the Indian companies Act provides the penalty for omitting to comply with certain of its provisions.

6. The directors may become personally liable for breach of trust, e. g., secret profits, receiving advance calls for their personal use etc.

7. They may also be liable for acting dishonestly, and in this case they are bound to make good any loss suffered by the company on account of their dishonesty.

8. The law as to liability of directors for negligence has been aptly summed up by Lord Justice Cotton as below :—

“The directors are confidential agents with liabilities of trustees; but they have a large discretion and if they act bonafide they are relieved, and are not liable for want of Judgement or errors if they make a payment which is not in fact for the purposes of the company”.

A director would, however, be liable if he is guilty of gross negligence, but the burden of proving that the non-performance of any particular acts amounts to such negligence rests on him who alleges it.

Under section 86—C, a director may become personally liable even for simple negligence. When they do not act within the province of their powers and with reasonable skill and diligence,

they shall be liable for any loss caused to the company, but they will not be liable for mere errors of judgement if they act bonafide and for the benefit of the company. If the directors delegate their powers to managing agents who misconduct the affairs of the company, certainly the directors will be liable for negligence. Any agreement with the company or any clause in the articles for affording relief, or exemption from, or indemnity against liability to any director, manager or officer or any auditor of the company is void under sec. 86—C.

9. Directors may also become liable for wilful wrong or default or wilful neglect. A director is here liable for misfeasance, i. e., a breach of duty which causes loss to the company. Misfeasance is something more than negligence: it also constitutes a breach of trust. While the company is a going concern, the remedy is by an action at law but after liquidation has commenced, proceedings may be taken under sec. 235. If, in the course of winding up, it appears that there has been misfeasance or breach of trust, the Court may on the application of liquidator or any creditor or contributory examine into the conduct of such person and compel him to pay damages. A director, who has been rendered liable is, however, entitled to contribution from his co-directors equally liable.

10. In certain circumstances, the directors may become criminally liable. Under sec. 236, they are liable to fine and imprisonment for destruction or falsification of books, accounts etc. Under sec. 237, they are liable to prosecution by the Court during the winding up of a company, if they are guilty of a criminal offence.

11. Last, but not the least, the directors may also become liable to fine if they do not comply with certain provisions of law.

CHAPTER IX.

LAW RELATING TO OTHER COMPANY OFFICERS

Managing director :

A managing director is an ordinary director entrusted with special powers. He is in no way a servant or clerk of the company, but like other directors he is the agent of the company for carrying on its business. Of course, he stands on a higher footing than an ordinary director. The Articles usually provide for the appointment of a managing director, and in this connection regulation 72 of Table A runs as follows :—

“The directors may from time to time appoint one or more of their body to the office of managing director or manager for such term, and at such remuneration (whether by way of salary or Commission, or participation in profits or partly in one way and partly in another) as they may think fit, and a director so appointed shall not, while holding that office, be subject to retirement by rotation or taken into account in determining the rotation of retirement of directors, but his appointment shall be subject to determination ipso facto if he ceases from any cause to be a director or if the company in general meeting resolves that his tenure of the office of managing director or manager be determined.”

It may, however, be noted that such appointment can be made only by the directors and the shareholders cannot interfere. Again, the directors may appoint a managing director for life and if the directors so appoint him for life in pursuance of their powers, the company cannot dismiss him, and, in case of his dismissal, he will be entitled to damages. The appointment of a managing director, however, ceases after the winding up order and consequently an appeal by him against the order of appointment of official liquidator does not lie.

The powers of a managing director are usually specified by the directors at the time of his appointment. He is, however, incompetent to forfeit shares, as Board of directors alone can forfeit them. The duties of a managing director are of a higher standard than an ordinary director.

Manager :

Under sec. 2 (9), Manager means a person who, subject to control and direction of the directors, has the management of the

whole of the affairs of the company, and includes a director or any other person occupying the position of manager, no matter what the name, and whether or not he is under contract of service.

The salient points of difference between a manager and an agent are as follows :—

MANAGER	MANAGING AGENT
1. A manager is a person who, subject to the control of directors, has the management of the whole affairs of a company, whether he is under a contract of service or not. Thus a director who actually manages a company without any contract of service is a manager. A Manager must be a mortal person, man or woman. 2. A manager cannot assign his office without the sanction of a special resolution of the company (sec. 86—B).	1. A managing agent means a person, firm or company entitled to the management of whole affairs of a company, by virtue of an agreement with the company and under the control of directors, except to the extent, if any, otherwise provided for in the agreement (sec. 2) (1). 2. A managing agent may transfer his office, if the transfer is approved by the company in general meeting (sec. 87—B).

The articles usually provide for the appointment of a manager and the powers that may be delegated to him. If, however, they are silent on these points, he may be appointed under a contract of service and the directors may delegate to him such of their powers as in a similar business are usually entrusted to a manager.

The relations between a company and its manager are regulated more or less, by the law applicable between master and servant. A manager is essentially the agent and servant of the company, and if he is guilty of any misconduct, in consistent with his duty towards his master, he is liable to dismissal. As regards duties, a manager is bound to attend to the details of the business of the company.

Besides this, he has certain statutory duties also; some of the more important of such duties are as below :—

- (1) Duty to sign a copy of annual list and summary, etc., to be filed with the registrar.
- (2) To sign profit and loss a/c and balance sheet.
- (3) To make the declaration verified by affidavit in case of a banking company.
- (4) To make memorandum of terms of contract in which company is an undisclosed principal.
- (5) To send information to registrar as to mortgages, charges, etc. and to maintain proper registers.
- (6) To see that securities deposited by the company's employees and proceeds of Employee's Provident Fund are properly applied and invested.

MANAGING AGENT

The institution of managing agents has received a statutory recognition by the Indian Companies Amendment Act of 1936, which has added sections 87 A to 87 I in this respect, while sec. 2 (1) (9—A) has defined the term “Managing Agent” for the first time.

Definition :

Section 2 (9—A) defines a managing agent as “a person, firm or company entitled to the management of the whole affairs of a company by virtue of an agreement with the company, and who is under the control and direction of the directors, except to the extent, if any, otherwise provided for in the agreement.

Appointment and duration :

Under sec. 87—B (f), the appointment of the managing agent is not to be valid without the sanction of the company in general meeting but the appointment made prior to the issue of the prospectus or statement in lieu of prospectus is exempt from such sanction.

According to section 87—A, public companies and their private subsidiaries are prohibited from appointing managing agents to hold office for more than 20 years at a time; and all managing agencies existing on 15th January, 1937 will automatically terminate within 20 years after that date. They may, however, be re-appointed to such office after the expiry of the said term or even before

the expiry of the said term of 20 years and in this case, the following two provisions hold good :—

(1) The termination of his office shall not take effect by virtue of the provision aforesaid until all money payable to him for loans made to or remuneration due up to the date of such termination from the company have been paid.

(2) The managing agent whose term of office is terminated by virtue of the aforesaid provision shall, upon such termination, be entitled to a charge upon the assets of the company by way of indemnity for all liabilities or obligations properly incurred by him on behalf of the company subject, however, to existing charges and incumbrances, if any.

Section 87—AA* further restricts the extension of term of office of managing agents, and provides as below :—

“In the case of a company managed by a managing agent; any amendment in the articles of or any variation in any agreement with, the company which purports to extend, or has the effect of extending, the term of office of a managing agent holding office as such on the 21 st. day of July, 1951, shall, notwithstanding anything to the contrary contained in any other provision of this Act or in the articles or agreement, be void unless approved by the Central Government, provided that nothing contained in the section shall apply to a private Company unless it is subsidiary Company of a public Company”. Its clear effect is that *now no extension of the office of managing agent can be made without the prior approval of the Central Government*. Further, the new section 87—C C provides that now (i. e., after 21 st. July, 1951) no fresh appointment or a reappointment of a managing agent can be made without the approval of the Central Government, and if made without such approval, it shall be void. This new section, however, does not apply to a private Company, unless it is a subsidiary of a public Company.

Remuneration :

Section 87—C provides that after 15th January, 1937, when any company (other than a private Company which is not the subsidiary of any public Company) appoints or reappoints a managing agent, his remuneration must be based on a fixed percentage of the net annual profits calculated after allowing for interests on

*Inserted by the Indian Companies Amendment Act, 1951

loans and depreciation, but before any deduction in respect of income-tax or interest on debentures. If the managing agent's remuneration is to be calculated on any other basis, a special resolution of the Company is required. A provision may, however, be made in the managing agency agreement for a minimum payment in case of low or inadequate profits, together with an office allowance. It is very important to note in this connection that prior to 21st July, 1951, remuneration in any other way could be fixed with the sanction of a special resolution of the Company; but *now the approval of the Central Government is also essential*. According to section 87—C C, after July 21, 1951, any amendment in the articles of, or any variation in any agreement with, the Company which purports to increase, or has the effect of increasing, whether directly or indirectly, the remuneration of the managing agent of a public Company, or of a private Company which is a subsidiary of a public Company shall be void unless approved by the Central Government.

Powers :

From the definition of the term “managing agent”, it is clear that they are entitled to the management of the whole affairs of a Company by virtue of an agreement with it, and they can also be independent of the control and direction of the directors in such matters as may be specified in the agreement.

Limitation of powers :

(1) Under section 87—G, directors are prohibited from delegating to managing agents the power to issue debentures, and under the same section the managing agents cannot invest the funds of the Company without the authority of the directors.

(2) Section 87—H, provides that a managing agent shall not on his own account engage in any business which is of the same nature as and directly competes with the business carried on by a subsidiary Company of such Company.

(3) Under section 87—I, the number of directors of a public Company appointed by the managing agents shall not exceed $\frac{1}{3}$ of the total number of directors, notwithstanding anything contained in the Company's articles.

(4) Under section 86—C, a managing agent is prohibited from contracting out of his legal responsibilities.

(5) Under section 87—F, a company other than an investment company is not to purchase shares and debentures of any company under management by the same managing agent, unless the purchase has been previously approved by the unanimous decision of the Board of directors of the purchasing company.

Restriction on authority :

(1) REMOVAL—Under section 87—B (a), a company may remove a managing agent by an ordinary resolution passed at a general meeting if he is convicted of a non-bailable offence relating to the affairs of the company. He is, however, protected, since he will not be liable to eviction if he dismisses the offending partner, director or other officer. It shall not be out of place to mention under this head that a managing agent may also be removed by the company under the common law on the ground of pecuniary misconduct, negligence, incompetence and permanent disability. It must, however, be noted here that if managing agents are removed by shareholders before the expiry of their term of office, compensation is usually payable to them in accordance with their agreements, and this fact is often a serious obstacle in the way of their removal.

(2) VACATION OF OFFICE—An undischarged insolvent cannot act as a managing agent, and consequently the office of the managing agent shall be vacated, if he is declared as an insolvent (87—B (b)). According to section 87—B (c), the managing agent contract is also terminated on the company being wound up, but the managing agent does not thereby lose his right to receive compensation for the premature termination of his contract, unless the winding up is due to his negligence or default, but not incompetence.

(3) TRANSFER OF OFFICE—According to section 87—B (c), a managing agent cannot transfer his office unless the transfer is approved by the company in general meeting and according to section 87—B B, in the case of a public company, also by the approval of the Central Government.

(4) TRANSFER OF REMUNERATION—Under section 87—B (d), the assignment of remuneration if made voluntarily by the managing agent is void, but a compulsory sale of such remuneration at the instance of a creditor is not affected.

(5) After 15th January, 1937 and prior to 21st July, 1951, removal and variation in contracts of the managing agents could be

made by the company in general meeting. But now after 21 st. July, 1951, to do this the approval of the company in general meeting and of the Central Government is necessary. The approval of the Central Government must be obtained even for the first appointment of managing agents, whether it be prior to the issue of prospectus or after such issue, and also in the case of his re-appointment.

THE NEW SECTION 87—B B

This section is designed to prohibit change in the controlling interest in the managing agency firm or company except with the prior approval of the Central Government. It provides that, "In the case of a public company managed by a managing agent which is a firm or a Company; on change in the constitution of the managing agent shall have effect unless approved by the Central Government, and every such firm or company shall cease to be entitled to act as such managing agent from the date of such change until the approval of the Central Government is obtained. The change requiring approval of the Government is deemed to take place :—

(a) In a managing agency firm, by a change among the partners whether caused by the retirement and replacement of any of the partners or by the introduction of a new partner.

(b) In the case of a company, by a change among the board of directors, or managers thereof, whether caused by retirement and replacement, of any director or manager, or by the introduction of a new director or manager, or by a change in the registered ownership of shares in the company; and

(c) Where the managing agent is a private company, by the conversion thereof into a public company. This provision takes away the effect of the proviso to sec. 87—B (c) which laid down that "in the case of a managing agents' firm a change in the partners thereof shall not be deemed to operate as a transfer of the office of managing agent, so long as one of the original partners shall continue to be a partner of the managing agents' firm".

But a change among partners of managing agency firm caused by the death or retirement by efflux of time of a partner; and if the managing agent is a company, a change among the board of directors, or managers caused by the death or retirement by efflux of time of any of them, or a change caused by the death of any shareholder of the managing agency company, shall not be deemed to be a change of constitution of a managing agent requiring

approval of the Central Government. Therefore, if any of these things happen the managing agent can continue to act as such without obtaining the approval of the Central Government. Moreover, it is laid down in sub-section (2) of section 87—B B, that where the change in the constitution of the managing agent which is a public company whose shares are dealt in or quoted on the principal stock exchanges of India, is due to a change in registered ownership of shares held therein, such a change shall not be deemed to be one requiring approval of Central Government, unless the Central Government by notification in the official Gazette directs that such managing agent shall cease to act as such until approval of the Central Government is obtained to the change; but such a notification will be issued only if the Central Government is of opinion that the change has affected or is likely to affect prejudicially the affairs of the company which is being managed by the managing agent.*

Loans to managing agents :

According to section 87—D, no public company or its public subsidiaries can make any loan out of their funds to their managing agents or to any partner of the firm if the managing agent is a firm, or to any member or director of the private company if the managing agent is a private company, companies, however, are allowed to maintain current accounts with their managing agents for purposes of their business

Contracts with Company :

Under section 87—D, a managing agent cannot enter into trading contracts with his company except with the consent of 3/4 of the directors present and entitled to vote on the resolution.

Inter-Company investments :

According to section 87—E, no public company can loan its money to any other public company under the management of the same managing agent. Closely allied to it is the question of the acquisition by one company of the shares and debentures of another company under the management of the same managing agent. In the event of any contravention of these provisions, any director or officer of the company making the loan or giving the guarantee who is the knowingly and wilfully in default, shall be liable to a fine not exceeding Rs. 1,000/- and shall be jointly and severally liable for

*Vide Indian Mercantile Law by M. C. Shukla Page 282—83.

any loss incurred by the company in respect of such loan or guarantee.

LEGAL ADVISER

The term "legal adviser" means and includes solicitors, pleaders, barristers and other legal advisers.*

The appointment of a legal adviser, like the appointment of any other officer of the company is usually secured by means of a contract with the company after its incorporation. Sometimes he is nominated in the articles of association.

The duty of a legal adviser is to advise the company in all matters referred to him for advice. He is merely an adviser with no authority and his advice may or may not be accepted. He may also attend the board meetings or be present at general meetings to advise the directors. Again it is the duty of the legal adviser to give the Advocate General or the Public Prosecutor, to whom the matter as to prosecution of any person guilty of an offence in relation to the company has been referred to by the Local Government under sec. 141—A of the Act, and who considers that the case is one in which a prosecution ought to be instituted, all assistance in connection with the prosecution which he is reasonably able to give (section 141—A)

CHAPTER X

OTHER COMPANY OFFICERS AUDITORS

Their qualifications :

According to section 144 (as amended by the Chartered Accountants Act, 1949), no person can be appointed or can act as the auditor of a public company or a private company which is the subsidiary of a public company, unless he is a Chartered Accountant ; provided that a firm whereof all the partners practising in India are Chartered Accountants may be appointed by its firm name to be auditor of a company and may act in its firm name. It may be stated here that a Chartered Accountant means a person who is a member of the Institute of Chartered Accountants of India constituted under the Chartered Accounts Act, 1949 and who is in practice.

Restrictions on appointment :

The following two restrictions are imposed on the appointment of auditors of companies.

(1) The following persons cannot be appointed as an auditor of a company.

- (a) A director or officer of the company ;
 - (b) A partner of such director or officer ;
 - (c) In the case of a public company or a private company which is the subsidiary of a public company, an employee of such director or officer ;
 - (d) Any person indebted to the company ;
- and (e) Any auditor who during his term of appointment, becomes indebted to the company, from the date of becoming indebted.

(2) Under the Auditor's Certificate Rules of 1932, if a person accepts a position as auditor previously held by some other Accountant without communicating with him, or accepts an appointment without first ascertaining from the company that the requirements of section 144(6) with regard to the giving of notices have been duly complied with, he becomes guilty of a breach of professional propriety, and his name is liable to be removed from the Register of Chartered Accountants.

Appointment :

The law relating to the appointment of auditors, as contained in section 140, is briefly summarised as below :—

1. **FIRST AUDITORS** :—Because the audit of the statutory report has been made compulsory under sec. 77, the first auditors may be appointed by the directors prior to the statutory meeting, and if so appointed, they shall hold office until the first annual general meeting, unless previously removed by a resolution of the members of the company in general meeting, in which case, such members at that meeting may appoint auditors.

2. **SUBSEQUENT APPOINTMENT** :—All subsequent appointments must be made at general meetings. But a person other than a retiring auditor cannot be appointed an auditor at a general meeting unless 14 day's notice of an intention to nominate that person as an auditor has been given to the company and a copy of the notice has been sent to the retiring auditor by the company. Further, it is the duty of the company to give seven days notice of the fact to its members. If at the annual general meeting, the retiring auditor is not reappointed and there is no other nomination before the meeting, no appointment of auditor will be made.

3. **APPOINTMENT BY GOVERNMENT** —If no appointment is made by the company at the annual general meeting, the provincial and or the central government may, on the application of any member of the company, appoint an auditor of the company for the current year.

4. **CASUAL VACANCY** —If an appointed auditor resigns or dies during his term of office, the directors may fill any casual vacancy in the office of auditor, but while such vacancy continues, the surviving or continuing auditor, if any, may act.

Note,—It shall not be out of place to mention in this connection that in the case of electric supply companies, the appointment and remuneration of the auditor are subject to the approval of the Provincial Government under the Indian Electricity Act, 1910.

Remuneration :

The remuneration of an auditor is determined by the party which makes the appointment, i. e., the directors, the company or the Provincial or Central Government as the case may be.

Rights and powers of auditors :

The rights and powers of an auditor according to section 145, are as follows :—

(1) Every auditor of a company shall have a right of access at all times to the books and accounts and vouchers of the company

and shall be further entitled to require from the directors and other officers of the company such information and explanation as may be necessary for the performance of the duties of the auditors. (sec. 145 (1)).

(2) The auditors of a company shall be entitled to receive notice of, and to attend, any general meeting of the company at which any accounts which have been examined or reported on by them are to be laid before the company. They may make any statement or explanation they desire with respect to such accounts.

Duties of Auditors :

(1) To acquaint with obligations under the articles and the act :—

It is the first and foremost duty of the auditors to acquaint himself with his statutory duties which are mentioned in the following paragraphs. He must also make himself familiar with the obligation or exceptional duties, if any, cast upon him by the articles of association of the company. Again, there may also be a special contract defining the duties and liabilities of the auditors, and in such a case that contract governs the question.

(2) Statutory Duties :

The following duties are imposed by law upon the auditors of a limited company :—

(i) TO CERTIFY THE STATUTORY REPORT—Under sec. 77 (4), the auditor is required to certify the statutory report so far as it relates to the shares allotted by the company, the cash received in respect of such shares, and the receipts and payments of the company. This provision does not apply to the auditor of a private company.

(ii) TO REPORT ON PROSPECTUS :—Under sec. 93 (1 A) (i), when a company which has been carrying on business issues a prospectus, its auditor is required to give a report for the purpose of insertion in the prospectus with regard to the profits earned and the dividends paid by the company during the last three years.

(iii) TO REPORT TO SHAREHOLDERS :—Under section 145 (2), an auditor of a company is to make a report to the members of the company on the accounts examined by him and

on every Balance-Sheet and Profit and Loss Account laid before the company in general meeting during his tenure of office. This report, besides other things necessary in a particular case, must expressly state :—

(a) Whether or not he has obtained all the information and explanation required by him ;

(b) Whether or not in his opinion the balance sheet and the profit and loss account are drawn up in conformity with the law ;

(c) Whether or not such balance sheet exhibits a true and correct view of the state of the company's affairs according to the best of his information and the explanations given to him, and as shown by the books of the company ;

(d) Whether or not in his opinion books of account have been kept by the company as required by law. If any of the above matters is answered in the negative or with qualification, the auditor must state the reason of such answer. Default to comply with the above conditions will render the auditor liable to a fine extending to 100/-

(iv) TO REPORT IN CASE OF WINDING UP :—Under section 207 (2), an auditor of a company is required to make a report on the company's affairs in support of the directors' declaration of the company's solvency, where it is proposed to wind up the company voluntarily and where it is desired to have a member's voluntary winding up.

(v) TO ASSIST ADVOCATE GENERAL :—Under sections 141-A and 237 (7), an auditor (past or present) of a company is bound to give all possible assistance to the Advocate General in connection with a prosecution of directors, etc.*

Although the statutory duty referred to above is not absolute and depends upon the information given and explanation furnished to the auditors, so that there is an abundant scope for discretion, yet that does not exempt them from the duty of examining matters for themselves. He is not to be a legal expert. He must be a honest and must exercise reasonable skill and care, otherwise he may be sued for damages. He must be a good watch-dog, be

* Note :—These duties of auditors are imperative, and no limit can be placed upon them by a company's Memo. or articles, although they can be enlarged by these documents.

alert and careful, and ascertain the true position of the company's affairs. But at the same time he is not an insurer, and does not guarantee the correctness of the books, as long as he has exercised reasonable care and skill in making enquiries and investigations. An auditor is not justified in omitting to make personal inspection of securities that are in the custody of a person with whom it is not proper that they should be left. As regards the extent of the duty to make reasonable and proper investigation, Lopes, L. J. observed as below .—

“Auditors must not be made liable for not trackling out ingenious and carefully laid schemes of fraud, when there is nothing to arouse their suspicion and when those frauds are perpetrated by tried servants of the company and are undetected for years by directors.” Thus the auditors are not bound to exercise more than reasonable care and skill in the discharge of their duty. Mr. Lopes further observes :—“It is the duty of an auditor to bring to bear on the work he has to perform that skill, care and caution which a reasonably competent, careful and cautious auditors would use. What is reasonable skill, care and caution, must depend upon the particular circumstances of each case. An auditor is not bound to be detective or as was said to approach his work with suspicion or with foregone conclusion that there is something wrong. He is a watch-dog, but not a blood hound. He is justified in believing tried servants of the company in whom confidence is placed by the company. He is entitled to assume that they are honest and to rely upon their representations, provided he takes reasonable care. If there is anything calculated to excite suspicion he should prove it to the bottom ; but in the absence of anything of that kind he is only bound to be reasonably cautious and careful.”

The duties of the auditors have been ably summed up by Lindley, L. J. in the following words :—

“It is no part of auditors’ duty to give advice, either to the directors or shareholders as to what they are to do. An auditor has nothing to do with the prudence or imprudence of making loans with or without security. It is nothing to him whether the business of the company is being conducted prudently or imprudently, profitably or unprofitably. It is nothing to him whether dividends are properly or improperly declared, provided he discharges his own duty to the shareholders. His business is to ascertain and state the

true financial position of the company at the time of the audit and his duty is confined to that but then comes the question, how is he to ascertain that position? The answer is; by examining the books of the company. But he does not discharge his duty by doing this without enquiry and without taking any trouble to see that books themselves shew the company's true position. He must take reasonable care to ascertain that they do so. Unless he does this, his audit would be worse than an idle farce, assuming the books to be so kept as to show the true position of a company, the auditor has to frame a balance sheet shewing that position according to the books and to certify that the balance sheet presented is correct in that sense. But his first duty is to examine the books, not merely for the purpose of ascertaining what they do shew, but also for the purposes of satisfying himself that they shew the true financial position of the company. An auditor, however, is not bound to do more than to exercise reasonable care and skill in making enquiries and investigations. He is not an insurer; he does not guarantee that the books do correctly shew the true position of the company's affairs. He does not even guarantee that his balance sheet is accurate according to the books of the company. If he did he would be responsible for error on his part, even if he were himself deceived without any want of reasonable care on his part, say, by the fraudulent concealment of a book from him. His obligation is not so onerous as this. Such I take to be the duty of an auditor; he must be honest, i. e., he must not certify what he does not believe to be true, and he must take reasonable care and skill before he believes that what he certifies is true. What is reasonable care in any particular case, must depend upon the circumstances of that case. Where there is nothing to excite suspicion, very little enquiry will be reasonably sufficient and in practice I believe, business men select a few cases at haphazard, see that they are right, and assume the others like them are correct also. Where suspicion is aroused more care is obviously necessary but, still, an auditor is not bound to exercise more than the reasonable care and skill, even in a case of suspicion, and he is perfectly justified in acting on the opinion of an expert where special knowledge is required".

Liabilities of Auditors :

(1) Under section 145 (5), if any auditor's report does not comply with the requirements of section 145, every auditor who is

knowingly and wilfully a party to the default is liable to a fine not exceeding Rs. 100/-.

(2) For any misfeasance and breach of trust in relation to the company, an auditor, who is formally appointed by the articles or under sec. 144 of the Act is, as an officer of the company, liable under sec. 235 of the Act (i. e , in the winding up of the company), and may be ordered by the Court to make good any loss suffered by the company. A person merely called in to audit the accounts pro hac vic is not, however, an officer of the company and is not, therefore, liable for misfeasance under sec. 235.

(3) The auditors are also liable for prosecution under sections 236 and 237 of the Act, for falsification of the books of the company or for any offence in relation to the company, discovered during to course of winding up.

(4) An auditor will be liable for ultra vires and illegal payments by directors prior to audit, if passed by him as good.

CHAPTER XI.

LAW RELATING TO HOLDING AND FOREIGN COMPANIES

Holding and subsidiary companies :

As already stated elsewhere in this book, where a company holds shares in another company directly or through a nominee and :—

(1) The amount of shares held is more than 50% of the issued share capital of the other company except where the shares are held as security by a company the ordinary business of which is the lending of money, or

(2) The share holding is such as to entitle the company to more than 50% of the voting power in the other company; or

(3) The company has power directly or indirectly to appoint the majority of the directors of that other company, then this latter company is called a *subsidiary company*, and a *holding company* is one which has such an interest in one or more subsidiary company.

Rights of members of holding company :

The rights conferred by section 132—A on the members of a holding company regarding the affairs of its subsidiaries are as below :—

(1) Along with the annual accounts of the holding company, its shareholders must also be supplied with the annual accounts of each subsidiary account, hence the last Balance Sheet, Profit and Loss account and the Auditor's Report of each subsidiary company should also be attached to the balance sheet of the holding company.

(2) There should also be annexed to the Balance Sheet of the holding company a statement signed by the same persons who are required to sign the Balance Sheet of the holding company and showing :—

(I) How the profits and losses of a subsidiary company (or the aggregate profits and losses where there are two or more subsidiary companies) have been dealt with in the accounts of the holding company; and

(II) To what extent provision has been made for the losses of any subsidiary company.

(3) In case the auditors' report of any subsidiary company is qualified in any respect, the statement to be annexed to the Balance Sheet of the holding company must contain particulars of the manner in which the auditors' report is qualified.

(4) The holding company may by a resolution authorise representatives named in the resolution to inspect the books of account kept in accordance with sec. 130 by any subsidiary company.

(5) The members of a holding company may appoint, by passing a special resolution, inspectors for investigating the affairs of a subsidiary company.

FOREIGN COMPANIES

(Sections 277—277—E)

Requirements as to companies established outside India :

Every company incorporated outside India, which establishes a place of business in India, must within a month of its doing so file with the registrar of the state in which such place of business is situated the following information :—

(1) A certified copy of the charter, statutes or memorandum and articles of the company, or other instrument constituting or defining the constitution of the company, and if the instrument is not written in the English language, a certified translation thereof;

(2) The full address of the registered or principal office of the company;

(3) A list of the directors and manager, if any, of the company;

(4) The names and addresses of some one or more persons resident in India authorised to accept on behalf of the company service of process and any notices required to be served on the company;

(5) The full address of that office of the company in India which is to be deemed the principal place of business in India.

Particulars of any alteration of the above must also be filed with the Registrar within the prescribed time. Such a company is also required to comply with the following provisions, if its liability is limited :—

(1) It must make out a Balance Sheet every Year containing the prescribed information and file three copies thereof with the registrar.

(2) It must state the country in which it is incorporated in every prospectus inviting subscriptions for shares or debentures in India.

(3) It must state its name and the country in which it is incorporated on all official publications.

(4) It must conspicuously exhibit on every place where it carries on business in India its name and the country in which it is incorporated.

(5) The fact regarding the limited liability must also be stated in every prospectus and in all official publications and must be exhibited in every place where it carries on business.

If any such company fails to comply with any of the above requirements, the company, and every officer or agent of the company, shall be liable to a fine not exceeding Rs. 500/- or, in the case of a continuing offence, Rs. 50/- for every day so long as the default continues.

Selling shares or debentures in India :

According to section 277—A, it is not lawful for any person :—

(1) To circulate in India the prospectus of a foreign company unless :—

(a) Before its issue or circulation, a copy thereof, certified by the chairman and two other directors of the company as having been approved by resolution of the managing body, has been delivered for registration to the registrar;

(b) The prospectus states on the face of it that the copy has been so delivered and

(c) The prospectus is dated; or

(2) To issue to any person in India a form of application for shares in or debentures of such a company or intended company, unless the form is accompanied by a prospectus.

The prospectus of a foreign company must contain the following particulars :—

(1) The objects of the company,

(2) The instrument constituting or defining the constitution of the company;

(3) The law under which the company is incorporated;

(4) An address in India where the said instrument and the law can be inspected;

(5) The date on which and the country in which the company was incorporated;

(6) Whether the company has a place of business in India and, if so, the address.

Provided that the information contained in points (1) to (4) need not be given if the prospectus is issued more than two years after the date on which the company was allowed to commence business (sec. 277—B).

Again, under the same section, if the prospectus is issued by a company already carrying on business it must also contain :—

(i) An auditors' report, and

(ii) An accountant's report.

Under sec. 277—C, it is not lawful for any person to go from house to house offering shares of a company incorporated outside India for subscription or purchase to the public or any member of the public. In other words share-hawking is unlawful and any person acting in contravention of this section is liable to a fine up to Rs. 100/-. To go from house to house means a physical contract with the residences approached, therefore, oral contracts by telephone must come within this prohibition.

CHAPTER XII

WINDING UP OF COMPANIES

Introduction :

A company once incorporated under the Indian Companies Act, cannot die a natural death. But it does not mean that its existence is necessarily perpetual. A joint stock company is created by law, and it is effaced by law. There are three distinct ways in which the personality of a company is dissolved :—

- (i) By winding up ;
- (ii) By its name being struck off by the Registrar ; and
- (iii) By being dissolved by an order of the court under sec. 153-A.

WINDING UP OF COMPANIES

The term 'winding up' stands for a proceeding by means of which the dissolution of a company is brought about. In the course of winding up the assets of the company are collected and realised and applied in payment of its debts, and when these are satisfied, the surplus assets are returned to the contributories in order to adjust their rights. There is no such thing as insolvency for a company, but winding up proceeding may be adopted for other purposes, e. g , re-incorporation for better management. Another synonym for a 'winding up proceeding is "Liquidation", and during the course of winding up, the company is said to be in liquidation and the work of liquidation is carried on by the Liquidator.

Modes of winding up :

The law relating to winding up is contained in sections 155-245. There are three different modes of winding up :—

- (1) Compulsory winding up ;
- (2) Voluntary winding up and
- (3) Winding up under the supervision of the court or supervisory winding up.

1. Compulsory Winding Up :—

According to section 162, a company may be wound up compulsorily under any of the six circumstances, viz, :—

- (i) When the company has passed a special resolution to be

wound up by the court. A company may be wound up for any cause whatever if a special resolution is passed for this purpose.

(ii) When default is made in filing the statutory report or holding the statutory meeting.

(iii) When the company does not commence business within a year from its incorporation or suspends its business for a whole year. The power of the court to wind up a company on this ground is discretionary, and will not be exercised unless there are indications that the company has no intention of continuing business. Again, if the suspension is due to temporary or unavoidable causes, the court will not order a winding up. Also, a company will not be wound up only because it has ceased to carry on one of several business, unless that business is the main object of the company. A company that has amalgamated with another company also cannot be wound up.

(iv) When the number of members falls below seven, or in the case of a private company below two. In such a case, usually the court does not interfere, but leaves the company to go into voluntary liquidation.

(v) When the company is unable to pay its debts. Under sec. 163, a company is deemed to be unable to pay its debts.

(a) If a creditor or to whom the company owes more than Rs. 500/- has served on the company a demand for payment and the debt has not been paid, secured or compounded within three weeks ; or

(b) If an execution on a judgement remains unsatisfied ; or

(c) If it is proved to the satisfaction of the court that the company cannot pay its debts including the contingent and prospective liabilities. The company would be wound up if it is unable to pay its current demands even though the assets when realised would exceed liabilities, because it is commercially bankrupt. Also, where its assets are locked up and it is running at a loss.

(vi) When the Court is of opinion that it is just and equitable that the company should be wound up. In this case the Court has very wide power and winding up orders have been given :—

(a) Where the whole object of the company was fraudulent

(b) Where the substratum of the company was gone. Thus where the principal object of the company was to acquire a particular gold mine, the title to the gold mine having failed,

the substratum was gone and the company was ordered to be wound up.

(c) Where there is a complete deadlock in the management.

(d) Where the majority of shareholders have forced a scheme on the minority.

Who may petition ?

Under section 166, the following persons are entitled to apply to the court for the winding up for a company :—

- (i) The company ;
- (ii) The Creditor ;
- (iii) The Contributory ;
- (iv) All or any of those parties, together or separately ;
- (v) The Registrar.

(1) **PETITION BY COMPANY** :—Petition to the Court by a company for its winding up will be made by its directors, when it has passed a special resolution for this purpose.

(2) **PETITION BY CREDITORS** —A creditor, including contingent and prospective creditor, may petition. The Court is bound as against the company to make a winding up order if the creditor can prove that he has an undisputed debt and that the company is unable to pay its debts according to section 163. But the court may refuse to order a winding-up if the majority of creditors oppose it. A creditor whose debt is unliquidated cannot petition at all. A debenture holder may petition if the principal moneys are payable to him direct and not to the trustee of a debenture trust deed. Also, the assignee of a debt or part of a debt can petition, but not a creditor of a third party who by a garnishee order attached a debt due from the company to the third party. In the case of a petition by a contingent or prospective creditor the Court shall not hear the petition until such security for costs has been given as the Court thinks reasonable and until a prima facie case for winding up has been established to the satisfaction of the court.

(3) **CONTRIBUTORY'S PETITION** :—In the case of a petition by a contributory, the court is not bound to order a winding up. As a matter of fact a contributory cannot petition unless he has held his shares for at least 6 months during the 18 months preceding the petition, except :—

(a) When the shares in respect of which he is a contributory or some of them either were originally allotted to him ; or

(b) When the shares have devolved upon him through the death of a former holder ; or

(c) When the number of company's members has been reduced below the statutory minimum.

A petition for winding up on the ground of default in filing a statutory report, or holding a statutory meeting can be presented only by a shareholder and after the expiration of 14 days from the last day on which the meeting ought to have been held.

A fully paid shareholder can petition. A member whose calls are in arrear can also petition. Similarly a contributory on the B List can petition. Any provision in the articles which deprives members of their right to petition for winding up is void.

(iv) REGISTRAR'S PETITION :—The Registrar is also not entitled to petition, but only on one ground that, from the financial condition of the company disclosed in its Balance Sheet or from the report of an inspector appointed under sec. 138, it appears that the company is unable to pay its debts. Petition by the registrar can be presented only with the prior sanction of the Central Government and the Central Government shall not give this sanction without giving the company an opportunity of being heard.

Procedure on compulsory winding up :

Winding up proceedings are commenced by a petition prepared and presented according to the rules and form made by the High Court under whose jurisdiction the company happens to be at the time of petition. The petition must contain the allegations and true facts, and must be supported by an affidavit of the petitioner. The winding up by Court shall be deemed to commence at the time of the presentation of the petition for the winding up (sec. 168). Further, an order for winding up shall operate in favour of all the creditors and of all the contributories of the company as if made on the joint petition of a creditor and of a contributory (sec. 167). After the petition but before the winding up order the Court may at its discretion at any time upon the application of the company or any creditor or contributory, restrain further proceedings against the company upon such terms as the Court thinks fit (sec. 169). Two companies cannot be wound up by the same order. The persons to be heard on the hearing of the petition are the company, creditor and any contributory.

Where several petitions are presented, they rank according to date of presentation.

On hearing the petition, the Court may (i) dismiss it with or without costs, (ii) adjourn the hearing conditionally or unconditionally, (iii) make any interim order or any other order that it deems just or (iv) make a compulsory order for winding up the company. Where the Court makes an order for the winding up of the company, it shall simultaneously appoint a liquidator who has to furnish security and thereafter conduct the liquidation work as Official Liquidator and Official Receiver will be informed forthwith (sec. 170). The Court may also settle the list of contributories, make calls and determine any question arising in the winding up on the application of the liquidator. When the order is made or a provisional liquidator is appointed, no suit or any other legal proceeding can be commenced or proceeded with against the company except by leave of the Court, and subject to such terms as the Court may impose (sec. 171). On the order being made a copy thereof has to be filed within a month by the company and the petitioner with the Registrar who will after noting the same in his book notify it in the official Gazette. Such order, under sec. 172, shall be deemed to be notice of discharge to the servants of the company, except when the business of the company is continued. The order is appealable, but only a liquidator, a creditor or a contributory can appeal. Ultimately, when the affairs of the company are completely wound up, the Court will make an order that the company be dissolved. It is the business of the liquidator to report this order to the Registrar who will register it and the company will then cease to exist ; but within two years of dissolution, the Court may, on the application of the liquidator or any other interested person, declare the dissolution to have been void.

2. Voluntary Winding Up :—

In the case of voluntary winding up, the company and its creditors are free to settle their affairs between themselves, with the liberty, however, to apply to the Court, if necessary. There are three circumstances in which a company may bound up voluntarily, and each mode requires a different form of resolution, viz :—

(1) When the period fixed for the duration of the company has come to an end or an event upon which the company is to be

wound up has happened, and the company has in general meeting passed an *ordinary resolution* to wind up.

(2) When the company passed a *special resolution* to wind up voluntarily, or

(3) When the company has passed an *extra ordinary resolution* that it cannot by reason of its liabilities carry on its business, and that it is expedient that the company be wound up (sec. 203).

According to section 204, a voluntary winding up commences from the date of the passing of the resolution for voluntary winding up. A proper notice required for the respective meetings must be given to all the members, and in the last-mentioned case it must state clearly that it is proposed to wind up the company because it cannot by reason of its liabilities carry on its business. An *extra-ordinary resolution* passed in pursuance of defective notice will be bad. Under sec. 206, when a resolution for winding up has been passed, a notice must be given by the company within ten days of the passing thereof by advertisement in the Official Gazette and also in some newspaper circulating in the district where the registered office of the company is situated.

Kinds of voluntary winding up :

There are two kinds of voluntary winding up—(i) Members' Voluntary Winding Up and (ii) Creditors' Voluntary Winding Up, and the law relating to each is as follows :—

Members' Voluntary winding up :

In the case of a members' winding up, a declaration of company's solvency has to be made. A majority of the directors may make and deliver to the Registrar a statutory declaration, verified by an affidavit to the effect that in their opinion the company will be able to pay its debts in full within three years from the commencement of the winding up. The declaration must be supported by a report of the company's auditors, and be filed with the Registrar (sec. 207). When such a declaration is made and filed with the registrar, the winding up is known as the Members' Voluntary Winding Up. The following provisions apply to such a winding up.

On the passing of the resolution for winding up, the company will in general meeting appoint a liquidator and fix his remuneration. On the appointment all the powers of the directors cease

except so far as the company in general meeting or the liquidator sanctions their continuance. If a vacancy occurs in the office of a liquidator, the company may in general meeting fill up the vacancy (sec. 208—A). Under sec. 208—B, a contributory or the continuing liquidator, if any, can call the meeting.

Creditors' voluntary meeting up :

Where in a voluntary winding up a declaration of solvency is not made and delivered to the registrar, it is known as Creditor's Voluntary Winding Up. In such a case, the company *must* call a meeting of the creditors for the same day as or on the next day after the meeting at which the resolution for voluntary winding up is to be proposed. The notice of the meeting must also be advertised. The directors must lay before the meeting of the creditors a statement of the position of the company along with a list of its creditors with the estimate of debt due to each. One of the directors will preside over the meeting. Default will render the company, the directors and officers liable to a fine upto Rs. 1,000 - (sec. 209—A).

The creditors and the company at their respective meetings may each nominate a liquidator, but the nomination of the creditors will prevail subject to an application to the Court (sec. 209—B). Further, the creditors may, at the same or subsequent meeting appoint a Committee of Inspection, consisting of not more than 5 persons; and in that event the company may also appoint not more than 5 persons to be members of the Committee, subject to the power of the creditor to disapprove of any persons so appointed. The Court may also give directions or appoint other persons (sec. 209—C). The Committee of Inspection or the creditors may fix the remuneration of the liquidator. If there is any vacancy, the creditors may appoint another liquidator. All the powers of the directors cease on the appointment of the liquidator, except so far as the Committee of Inspection or the creditors sanction the continuance thereof (sec. 209—D).

Procedure in voluntary winding up :

The following provisions apply to every voluntary winding up, whether members' or creditors' :—

(a) Subject to the payment of preferential creditors, the property of the company is applied first in discharge of its liabilities *pari passu*, and subject thereto is distributed among the members (sec. 211).

(b) The liquidator may exercise the same powers as those of official liquidator—some with the sanction of an extraordinary resolution of the company or with the sanction of the Court or the Committee of Inspection, and some without any such sanction (sec. 212).

(c) If from any cause whatever there is no liquidator acting, the Court may appoint a liquidator and it may, on proper cause being shown, remove a liquidator, however, appointed, and appoint another in his place (sec. 213).

(d) Every liquidator must within 21 days after his appointment, deliver to the registrar for registration a notice of his appointment in the prescribed form. Default will render him liable to a fine upto Rs. 50/- for every day during which the default continues (sec. 214).

(e) Any arrangement entered into between a company and its creditors shall be binding on the company if sanctioned by an extraordinary resolution, and on the creditors if acceded to by $\frac{3}{4}$ in number and value of the creditors. Further, any creditor or contributory may, within three weeks from the completion of the arrangement, appeal to the Court against it, and the Court may thereupon, as it thinks just, amend, vary or confirm the arrangement (sec. 215).

(f) The liquidator or any contributory or creditor may apply to the Court to determine any question arising in the winding up of a company. He has also the power to settle a list of contributories and to make calls (sec. 216).

(g) All expenses of winding up, subjects to the rights of secured creditors, are payable out of the assets of the company in priority to all other claims (sec. 217).

(h) The winding up of a company shall not bar the right of any creditor or contributory to have it wound up by the Court, but in the case of an application by a contributory, the Court must be satisfied that the rights of the contributories will be prejudiced by a voluntary winding up (sec. 218).

Well, as regards the procedure in voluntary winding up, it may be stated that the liquidator has to collect the outstandings of the company and pay off its debts as soon as possible. If the winding up continues for more than a year, the liquidator must summon a general meeting of the company and a meeting of the creditors at the end of the first year and of each successive year and

lay before the meetings an account of his doings. Default will render him liable to a fine upto Rs. 100/- (secs. 208—D and 208—G). When the affairs of the company are fully wound up, the liquidator must make up an account and call final meetings of the company and the creditors and lay the account before the meetings. Within a week after the meetings, the liquidator must send to the registrar a copy of the account and a return which will be registered, and on the expiration of three months from the registration, the company will be dissolved. The Court may, on the application of the liquidator or any other person interested in the affairs of the company, defer the date of dissolution for such time as it thinks fit. In the last case, the applicant must file within 21 days a copy of the order with the Registrar (secs. 208—E to 209—H). Dissolution thus reached cannot be reopened, except in the case of fraud, or under sec. 243, which provides that a Court may, within 2 years of the date of dissolution, on an application of the liquidator or any other person interested in the affairs of the company, make an order declaring the dissolution void, and thereupon such proceedings may be taken, as might have been taken if the company had not been dissolved.

DISTINCTION BETWEEN MEMBER'S AND CREDITOR'S WINDING-UP

MEMBERS' WINDING-UP	CREDITORS' WINDING-UP
1. In the case of a member's winding up, a declaration of company's solvency has to be made.	1. If in a voluntary winding-up, a declaration of solvency is not made and delivered to the Registrar, it is known as a Creditors' voluntary winding up.
2. There is no meeting of creditors in a member's winding up, and the liquidator nominated at the meeting of the company acts in the liquidators of its affairs.	2. In a creditor's winding up the directors are bound to convene a meeting of creditors for the day, or the day next following the day, on which there is to be held the meeting of the members at which the resolution to wind up is to be proposed.

DISTINCTION BETWEEN COMPULSORY AND VOLUNTARY WINDING-UP

NO.	BASIS OF DISTINCTION	COMPULSORY LIQUIDATION	VOLUNTARY LIQUIDATION
1	Mode of Institution	A compulsory winding up emerges on an order of the Court made on the petition of the company or creditors or contributories.	A voluntary winding up is instituted by a resolution of the company.
2	Date of commencement	A compulsory winding up commences from the date of the presentation of the petition.	A voluntary winding up commences from the date of passing the resolution to wind up.
3	Appointment of Liquidator	Here the liquidator is appointed by the Court.	Here the liquidator is appointed by the company in general meeting. In the case of creditor's voluntary winding-up, however, the creditors may appoint the liquidator, or they may assent to the company's nominee
4	Lists of contributories	Here the lists of contributories are settled by the official liquidator as an officer of the Court.	Here they are settled by the liquidator himself on his own responsibility.
5	Call	In this case calls are made on the contributories by the official liquidator as an officer of the Court.	In this case calls are made by the liquidator on his own responsibility.
6	Passing of Accounts	The accounts of an official liquidator are submitted to the Court which gets them audited.	Here the liquidator's accounts are passed in general meeting. In a creditors' winding up, of course, the accounts are also submitted to the creditors at an annual and final meetings.

7 Dissolution
of Com-
pany

In this case a com-
pany is dissolved by an
order of the Court when
its affairs have been
wound up completely.

Here, the company
is dissolved three months
after the notice of the
final meeting has been
given to the Registrar.

3. Supervisory Winding Up :—

Under section 221, when a company has by special or extraordinary resolution resolved to wind up voluntarily, the Court may make an order that the voluntary winding up shall continue, but subject to such supervision of the Court, and with such liberty for creditors, contributories or others to apply to the Court, and generally on such terms and conditions as the Court thinks fit. The application for the intervention of the Court will be made when there are irregularities or frauds in the voluntary winding-up.

While making an order on the application for supervision, the Court will have regard to the wishes of the creditors and the contributories. It will not, as a rule, make a supervision order on the petition of a contributory unless it is satisfied that the resolution for winding up was so obtained that the minority of shareholders were overborne by fraud or improper or corrupt influence.

In such a winding up, the Court has power to appoint an additional liquidator or remove the old liquidator and appoint a new one in his place. Generally, the Court permits the old liquidator to continue if there is no complaint against him. The effect of the supervision order is that the liquidator may, subject to any restrictions imposed by the Court, exercise all his powers without the sanction of the Court in the same manner as if the company were being wound up altogether voluntarily. All the proceedings will be stayed as in a compulsory winding-up, unless permitted by the Court.

Liquidators in compulsory winding-up :

As soon as the winding-up order is made by the Court, it will appoint one or more persons to be called Official Liquidators for the purpose of conducting the proceedings in winding-up and for performing such duties in reference thereto as the Court may impose. But if no liquidator is appointed, section 17—A provides that the Official Receiver attached to the Court will automatically become² the Official Liquidator. The Court may make such an

appointment provisionally at any time after the presentation of a petition and before the making of an order for winding up. Where more than one liquidator has been appointed, the Court may declare whether all or one will act as such, and may also require them to give security.

Under section 175, the liquidator must, on appointment, notify the fact of his appointment to the registrar before he can act. On appointment, the liquidator takes into his custody all the property and effects of the company, and those are deemed to be in the custody of the Court. It should be noted here that the liquidator merely acts as a trustee for all persons who were creditors of the company at the date of the winding up. The liquidator, in fact, represents both the company and the creditors (section 178). Section 176 provides that an official liquidator may resign or be removed by the Court on due cause shown. Any vacancy in the office of an official liquidator shall be filled up by the Court; and until it is so filled up, the official Receiver shall act as liquidator. The remuneration payable to the official liquidator whether by way of percentage or otherwise, is fixed by the Court.

Powers of official liquidator :—

According to section 179, an Official liquidator has power, with the sanction of the Court, to do the following things :—

(1) To institute and defend suits or prosecution in the name of the company ;

(2) To carry on the business of the company so far as may be necessary for the beneficial winding up.

(3) To sell movable and immovable property in any suitable manner.

(4) To execute and seal documents and deeds on behalf of the company.

(5) To prove, rank and claim in the insolvency of a contributory.

(6) To draw bills of exchange, hundies and promissory notes—these having the same effect as if drawn by the company.

(7) To raise money on the assets of the company.

(8) To take out in his official name letters of administration to any deceased contributory.

(9) To appoint an advocate, attorney or pleader entitled to appear before the Court to assist him, but if the liquidator is an

attorney, he can appoint his partner only if the latter agrees to act without remuneration (section 681), and

(10) To do all things necessary for the winding of the company and distributing its assets (section 179)

*Note :—*The Court may provide by an order that the official liquidator may exercise any of the above powers (except the 9th one) without the sanction of the Court.

Duties of Official Liquidator :

The duties of an Official liquidator are as follows :—

(1) He must take into his custody and control all the books, documents and the assets of the company (section 178).

(2) He must have regard to any directions given by resolution of the creditors or contributories at any general meeting, or by the Committee of Inspection, directions of the creditors or contributories over-riding those of the Committee, where there is a conflict (Section 183).

(3) He may summon general meetings of the creditors or contributories for the purpose of ascertaining their wishes and must do so if requested in writing to do so by 1/10 in value of the creditors or contributories as the case may be (Section 183 (2)).

(4) He may apply to the Court for direction in relation to any particular matter arising in the winding up (Section 183 (3)).

(5) He must use his own discretion in the administration of the assets of the company and in the distribution thereof among the creditors (section 183 (4)).

(6) Under section 182, he must keep in the prescribed manner, proper books for making entries or minutes of proceedings at meetings, and of such other matters as may be prescribed. All such books are to be open to the inspection of any creditor or contributory subject to the control of the Court.

(7) Under section 182, sub-section 2, he must present to the Court at least twice a year his account of receipts and payments in duplicate and duly verified by him. The Court shall have the account audited ; and for this purpose the official liquidator must submit to the Court the necessary vouchers. When the account is audited, one copy will be kept in the Court and the other copy shall be filed with the Registrar.

Statement to the liquidator :

According to the new section 177-A, where the Court has made a winding up order, a statement as to the affairs of the company verified by an affidavit, should be made out and submitted to the official liquidator. It should contain the following particulars, viz :—

- (a) the assets of the company, stating separately the cash balance in hand and at the bank; if any ;
- (b) the debts and liabilities ;
- (c) the names, residence and occupations of the creditors stating separately the amount of secured debts and unsecured debts, and in the case of secured debts, particulars of the securities, their value and the dates when they were given ; and
- (d) the debts due to the company and the names, residences and occupations of the persons from whom they are due and the amount likely to be realised therefrom.

Default in submitting a correct statement will render these persons liable to a fine upto Rs. 100/- for each day of default. The statement should be submitted within 21 days from the relevant date, or within such extended time as the liquidator or the Court may appoint.

Statement by the liquidator :

As soon as practicable after the receipt of the statement of affairs (and not later than four months from the date of the winding-up order), the official liquidator is required, under section 177-B, to submit to the Court a "Preliminary Report."

(a) as to the amount of capital issued, subscribed, and paid up, and the estimated amount of assets and liabilities, giving separately under the heading of assets particulars of :—

- (i) cash and negotiable securities ;
- (ii) debts due from contributories ;
- (iii) debts due to and securities, if any, available to the company ;
- (iv) moveable and immoveable properties belonging to the company ;
- and (v) unpaid calls ; and
- (b) if the company has failed, as to the causes of the failure ; and

(c) Whether in his opinion further inquiry is desirable as to any matter relating to the promotion, formation, or failure of the company, or the conduct of the business thereof.

If he thinks fit the official liquidator may submit a "further report" to the Court, stating the manner in which the company was formed, whether in his opinion fraud has been committed by any person in its promotion or formation by any director or other officer, and any other matters which in his opinion it is desirable to bring to the notice of the Court.

Committee of inspection :

It is a body of persons appointed in a compulsory winding-up to represent the interests of the creditors and contributories and to exercise a certain degree of control and supervision over the liquidator. The law with regard to it, as contained in section 178-A, is as follows :—

The official liquidator must, within a month from the date of the order for the winding-up of a company, convene a meeting of the creditors for the purpose of determining whether or not a committee of Inspection is to be appointed and who are to be the members of the committee, if appointed. Within a week from the date of the creditors meeting, the official liquidator should convene a meeting of the contributories to consider the decision of the creditors and to accept the same with or without modifications. If the contributories do not accept the decision of the creditors in its entirety, it shall be the duty of the official liquidator to apply to the Court for directions as to whether there shall be a Committee of Inspection and, if so, what shall be the composition of the committee, and who shall be members thereof.

The maximum number of members in a committee of inspection should not exceed 12 and the minimum is two. The committee should consist of creditors and contributories of the company or persons holding general or special powers of attorney from them in such proportions as may be mutually agreed upon by the creditors and contributories, or as, in case of difference, may be determined by the court.

The committee of inspection shall have the right to inspect the accounts of the official liquidator at all reasonable times. The committee shall meet at such times as they may from time to time appoint, and, failing such appointment, at least once a month, and the liquidator or any member of the committee may also call a meeting of the committee as and when he thinks necessary. The Committee may act by a majority of its members present

at a meeting, but it will not act unless a majority of the members are present.

A member of a committee may resign by a written notice given to the liquidator ; and a member shall vacate his office :—

- (i) If he becomes bankrupt ; or
- (ii) If he compounds or arranges with his creditors ; or.
- (iii) If he absents himself, from five consecutive meetings of the committee without leave.

A member of the committee may be removed by an ordinary resolution at a meeting of creditors if he represents creditors, or contributories if he represents contributories, of which seven days' notice has been given, stating the object of the meeting. If there is a vacancy in the committee, the liquidator must call a meeting of the creditors or contributories to fill the same.

Powers of the court :

Ordinary powers of the court in winding-up a company are as below :—

(1) To settle a list of contributories and to cause the assets of the company to be collected and applied in discharge of its liabilities.

(2) To require any contributory and any trustee receiver, banker, agent or officer of the company to surrender or transfer to the official liquidator any money, property or documents to which the company is entitled.

(3) To make an order on any contributory to pay any money due from him to the company, excluding any money payable by virtue of a call.

(4) To make calls on the contributories for the purpose of paying the debts of the company and for adjusting the rights of the contributories inter se.

(5) To order any person from whom money is due to the company to pay the same into the account of the official liquidator in a scheduled bank.

(6) To fix a time within which the creditors are to prove their claims.

(7) To adjust the rights of contributories inter se.

(8) To order the payment of liquidation expenses out of the company's assets in such order of priority as it thinks fit.

(9) To order the dissolution of the company when its affairs have been completely wound up.

The extra-ordinary powers of a court in the winding-up of a company are as below :—

(1) To summon before it any person known or suspected to have in his possession any property of the company.

(2) To order public examination of a promoter, director or other officer of the company, where fraud is suspected.

(3) To order for the arrest of a contributory or seizure of his property, if it is considered necessary.

LIQUIDATORS IN VOLUNTARY WINDING-UP

Powers of liquidator :

The liquidator may, under section 212 (1), in a voluntary winding up, with the sanction of an extra-ordinary resolution of the company in a member's voluntary winding up, and with the sanction either of the Court or of the Committee of Inspection in a creditor's winding-up, exercise the following powers —

1. To execute and seal documents and deeds on behalf of the company.

2. To prove in the insolvency of any contributory.

3. To draw B/E, hundies and P/N having the same effect as if drawn by the company.

4. To take out in his official name letters of administration to any deceased contributory,

Besides the above, the liquidator may, under sub sec. 2, exercise the following powers without any sanction referred to above, —

(1) To exercise all the other powers of an official liquidator.

(2) To settle the list of contributories and make calls.

(3) To summon general meetings of the company for obtaining its sanction by special or extra-ordinary resolution or for any other purpose.

Functions of voluntary liquidator :

The various functions of a voluntary liquidator are as follows :—

(1) To satisfy himself that the resolution for voluntary winding-up was validly passed and that a copy was duly filed with the registrar.

- (2) To file with the registrar a notice of his appointment.
- (3) To advertise in the official Gazette and in a local newspaper asking the creditors to meet at a certain place and time fixed by him within 21 days of his appointment, and also to tend such notice to each creditor.
- (4) To take possession of the company's assets and see that they are in tact.
- (5) To call by advertisement for the claims of creditors by a certain date and to approve the debts.
- (6) To prepare a list of debts and claims and send notices to contributories for the settlement of the list of contributories.
- (7) To settle the list of contributories on the date fixed for the purpose.
- (8) To look into all payments made during the three months immediately preceding the liquidation and satisfy himself that there has been no fraudulent preference.
- (9) To dispose of the assets of the company to the best advantage and collect so far as practicable all outstanding debts due to the company.
- (10) To apply the proceeds of realisation in the prescribed manner.
- (11) To make a call on the unpaid shares, if necessary.
- (12) To file returns at the end of first year and then every six months during the continuance of winding up.
- (13) To convene the annual general meeting of the company.
- (14) To call a general meeting at the end of winding up and lay before it the account of winding-up, and
- (15) To file within a week of this meeting a return to the registrar of the holding thereof. He must not make any secret profits and must keep the funds of the company in a scheduled bank.*

Disclaimer of property :

Section 230-A empowers the liquidator to disclaim any onerous property of the company. Under this section, the liquidator of a company may, with the sanction of the Court and by writing signed by him, at any time within 12 months from the commencement of winding-up, disclaim any of the following onerous property

* Extracted from "Indian Mercantile Law" by M C Shukla ; Page 344.

of the company :—Land of any tenure burdened with onerous covenants ; shares or stock in companies ; any other property which is unsaleable by reason of the possessor there of being liable to perform any onerous act or the payment of a sum of money in respect thereof.

The disclaimer operates to determine as from the date of the disclaimer all rights or liabilities of the company, but shall not affect the rights or liabilities of any other person. The liquidator is debarred from exercising his right of disclaimer if any person interested in the property requires him in writing to decide whether he will or will not disclaim, and the liquidator does not take any step in the matter within 21 days after the receipt of the application. Any person injured by the operation of a disclaimer is deemed to be a creditor of the company for the amount of the injury, and may prove for the amount as a debt in the winding up. The Court may also make an order for rescinding the contract on such terms as to payment by or to either party of damages for the non-performance of the contract or otherwise as the Court thinks just. Even if the liquidator does not exercise the right to disclaim, he does not render himself liable when he elects to perform a contract of the company.

DISSOLUTION ON BEING DEFUNCT

The second case in which a companies personality is dissolved, is by its name being struck off by the Registrar. Thus, according to section 247, where the registrar has reasonable cause to believe that a company is not carrying on business or in operation, he shall send to the company by post a letter inquiring whether the company is carrying on business or in operation. And if, within a month of sending the letter, he does not receive any answer thereto, he shall, within 14 days after the expiration of the month, send to the company by post a registered letter referring to the first letter and stating that no answer thereto has been received to the second letter within a month from the date thereof, a notice will be published in the Official Gazette with a view to strike the name of the company off the Register.

DISSOLUTION WITHOUT LIQUIDATION

If a company enters into an arrangement of reconstruction or amalgamation, entailing the transfer of its assets and undertaking to another company, the Court in sanctioning the scheme may

make an order, under section 153-A, for the dissolution of the company without winding. The procedure is that when a company is sought to be re-constructed or amalgamated, a special resolution for voluntary winding-up of the company is passed. The voluntary liquidator is given the power to transfer its undertaking and property to the transferee company and to receive, in consideration of the transfer, fully or partly paid up shares or any other interest or in addition to participate in the profits of the transferee company. Any such sale or arrangement shall be binding on the members of the transferor company.

Disposal of accounts on liquidation :

According to section 242 (1), when a company has been wound up and is about to be dissolved, the documents of the company and of the liquidator may be disposed of as follows :—

(a) In the case of a compulsory or supervisory winding-up, in such a way as the Court direct ; and

(b) In the case of a voluntary winding-up, in such a way as the company by extra-ordinary resolution directs.

Under sub sec. 2, after three years from the dissolution of the company, no responsibility will rest on the liquidator or any person to whom the custody of the documents has been committed, by reason the same not being forth-coming.

Consequences of winding-up as to shareholders :

In a company limited by shares, a shareholder is liable to pay full amount on the shares held by him, but nothing more. This liability of a shareholder continues even after liquidation; but, he is then described as a “contributory”. According to section 158, the term ‘contributory’ means every person liable to contribute to the assets of a company in the event of its being wound up, and, in all proceedings for determining and in all proceedings prior to the final determination of the persons who are to be deemed contributories, includes any person alleged to be a contributory. A holder of fully paid shares is a contributory in respect of adjustment of rights among the contributories themselves. According to section 156, every past or present member becomes a contributory, unless he can bring himself within the following exceptions :—

(a) In the case of a company limited by, shares, no contribution can be required from any member exceeding the amount,

if any, unpaid on the shares in respect of which he is liable as a past or present member.

(b) In the case of a company limited by guarantee, no contribution shall be required from any member exceeding the amount undertaken to be contributed by him to the assets of the company in the event of its being wound up. If such a company has a share capital, the limitation of liability will also extend to the amount remaining unpaid on his shares.

(c) A past member is not liable to contribute :—

(i) If he has ceased to be a member for one year or more before the commencement of winding up ; or

(ii) In respect of any debt of the company contracted after he ceased to be a member ; or

(iii) Unless it appears to the Court that the exceeding members are unable to satisfy the contributions required to be made by them.

Under section 159, the liability of a contributory shall create a debt payable at the time specified in the calls made on him by the liquidator. If a contributory dies, the liability to contribute passes to his legal representatives to the extent of properties which has come into their hands from the deceased shareholder ; and the surviving parceners of a contributory, who is a member of a Hindu joint family governed by the Mitakshara school of Hindu Law, shall be deemed to be his legal representatives; If a contributory is declared as an insolvent, his assignees shall be contributories, and the company may prove against the estate of the insolvent in respect of his liability to calls (Sections 160 & 161).

List of contributories :

On a winding up, a list of contributories is prepared and settled by the liquidator. There are two parts of the list :—

(i) A list, consisting of the present members, who are registered as members at the commencement of winding-up ; and

(ii) B list, consisting of passed members, who have ceased to be members within a year before the commencement of winding-up. Each list must distinguish between those who are liable personally and those who are liable as personal representatives.

The measure of liability of "A contributory is only one, viz ; the full amount unpaid on his shares. If the company is limited

by guarantee, he is liable for the amount undertaken to be contributed by him in the event of a winding-up, and if such company has a share capital, he is, in addition, liable to contribute the amount remaining unpaid on the shares held by him

The liability of the "B contributory" is created by the Act and is subject to the following limitations :—

(a) He is liable only to the extent to which the transferee of his shares has failed to pay them up in full ; and

(b) He is liable to pay only so much of this amount as is necessary to pay so much of the debts incurred while he was a member as remain unpaid after applying all the contributions of the A list contributories and all the assets of the company *pari passu* towards payment of all its debts, irrespective of the date when they were incurred.

Generally all the contributories contribute to the extent of the unpaid amounts including the cost of the winding up, even if they were induced to buy shares by fraud or misrepresentation ; but they may also have a right to damages against the managing agents, directors or other officers of the company. A contributory may, however, escape liability, if he had applied to have his name removed from the register before the winding up commenced ; and if the shares were purchased conditionally and the condition had not been fulfilled, he will not be liable, if the condition was precedent and he took prompt action.

Director contributory :

In the winding up of a limited company, any director, whether past or present, whose liability is unlimited, shall, in addition to his liability as an ordinary member, be liable to make a further contribution as if he were at the commencement of the winding-up a member of an unlimited company. But :—

(i) A past director shall not be liable to make such further contribution, if he has ceased to hold office for a year or upwards before the commencement of winding up ;

(ii) A past director shall also not be able to make such contribution in respect of any debt or liability of the company contracted after he ceased to hold office ;

(iii) Subject to the articles, he shall also not be liable to contribute as such unless the Court deems it necessary to require

that contribution in order to satisfy the debts and liabilities of the company, and the costs, charges and expenses of the winding-up (Section 157).

The liability to contribute is enforced by means of call by the voluntary liquidator himself, or by the Official Liquidator by sanction of the Court ; and as soon as a call is made, it becomes a debt payable in winding up. If the call is not paid, the liquidator may apply to the court for a "payment order" in summary proceedings, or may file a suit in the name of the company. This order can be enforced in the same manner as a decree.

As to creditors :

A company can never be adjudged as an insolvent. It might be unable to pay its debts, and in this sense, of course, it may be considered as bankrupt. As regards the rights of contributories, a distinction is to be made between solvent and insolvent companies. According to section 228, in every winding up, all debts payable on a contingency, and all claims against the company, present or future, certain or contingent shall be admissible to prove against the company, a just estimate being made, so far as possible, of the value of such debts or claims as may be subject to any contingency or some other reason do not bear a certain value. Thus, there is no difficulty in the case of a solvent company, as where the claims are proved they are paid. Under section 229, in the case of an insolvent company, the same rules prevail as to :—

- (i) the respective rights of secured and unsecured creditors ;
- (ii) debts provable ; and
- (iii) the valuation of annuities and future and contingent liabilities, as are in force under the law of insolvency.

Thus a secured creditor may either :—

- (i) rely on the security and ignore the liquidation altogether, or
- (ii) value his security and prove for the balance of his debt, or
- (iii) give up his security and prove for the whole amount.

Unsecured creditors of an insolvent company are paid in the following order :—

- (i) Preferential payments, and
- (ii) other debts *pari passu*.

But debts, in respect of which a rate of interest is paid varying with the profits of the company, are postponed until other debts are paid in full.

Preferential Payments :

In a winding up, the following debts are paid in priority to all other debts :—

(1) All revenue, taxes, cesses and rates, whether payable to the crown or to a local authority, due from the company at the relevant date and having become due and payable within 12 months next before that date. Crown debts other than those mentioned above have no priority.

(2) Wages of a clerk or servant for services rendered to the company within two months before the relevant date, and not exceeding Rs. 1,000/- for each clerk or servant.

(3) Wages of a labourer or workman for services rendered to the company within two months before the relevant date, and not exceeding Rs. 500/- for each labourer or workman.

(4) Compensation payable under the workman's Compensation Act of 1923 to any officer or employee of the company.

(5) Sums due to an employee from any fund mentioned by the company for the welfare of the employees, e. g , provident fund, pension fund etc.

(6) The expenses of an investigation held in pursuance of section 138.

(a) The expression "relevant date" means in the case of a company ordered to be wound up compulsorily, which had not been previously commenced to be wound up voluntarily, the date of winding-up order ; and

(b) in any other case, the date of the commencement of winding up.

These debts have priority over the claims of the holder of debentures having a floating charge on the assets of the company. If after the payment of liquidation expenses, there are not sufficient funds to discharge the entire above mentioned preferential debts, payment must be made rateably so far as the available funds permit. (Section 230).

Fraudulent Preference :

Under section 231, any transfer, delivery of goods, payment, execution or other act relating to property which would, if made or done by or against an individual, be deemed in his insolvency a fraudulent preference, shall, if made or done by or against a

company, be deemed in the event of its being wound up a fraudulent preference and be invalid accordingly. Any transfer or assignment by a company of all its property to transfer for the benefit of all its creditor is void. But, in order to prove a fraudulent preference under this section, it must be shown that :—

(i) The company was, at the date of transfer or payment, unable to pay its debts as they become due ;

(ii) The transfer or payment was in favour of a creditor and that it was made with a view to giving that creditor a preference over the other creditors ; and

(ii) The company went into liquidation within three months after the date of the transaction.

If any of these conditions is not fulfilled, the transaction will not be void as a fraudulent preference.

According to section 233, a floating charge on property and undertaking of a company, created within three months of the commencement of winding-up, shall, unless it is proved that the company immediately after the creation of the charge was solvent, be invalid except to the amount of any cash paid to the company in respect of charge with 5% interest thereon.

As to officers :

Section 196 provides for the public examination of the promoters, directors and other officers of a company which is being wound up by an order of the Court. Where the official liquidator has suspected that fraud has been committed, the court may order that any person, who has taken part in the promotion of the company shall attend and be publicly examined on oath as to the formation and business of the company and as to his conduct. The official liquidator shall take part in the examination, and any creditor or contributory may also take part therein.

Further, if any director, promoter, liquidator or other officer of the company has misapplied or retained money or property of the company, or has been guilty of misfeasance, or breach of trust, the Court may, on the application of the liquidator or of any creditor or contributory, examine into his conduct and order him to repay or restore money or property or to pay compensation (section 235).

Section 236 further provides that, if any director, manager officer (including auditor) or contributory of a company is

responsible for the destruction of falsification of any books or documents of the company with intent to deceive any person, he is liable to imprisonment upto seven years and is also liable to a fine.

Again, section 237 empowers the Court to direct the liquidator either to prosecute delinquent directors and officers of the company or to refer the matter to the Registrar. But before proceedings can be taken, the accused persons must be given an opportunity to make statement to the registrar and of being heard thereon. It is the duty of the liquidator and of every officer and agent of the company (past and present) other than the delinquent person to give to the Registrar all possible help in the prosecution.

As to servants :

A winding up order, under section 172 (3), operates as a dismissal or discharge of the servants of the company.

As to proceedings against the company :

After the winding-up order is passed, all proceedings against the company must cease, unless the Court gives special permission for their continuance. Under section 232, any attachment distress execution put in force against the assets of the company after commencement of winding up is void.

As to costs :

If the company, while in liquidation, brings or defends an action and is ordered to pay costs, they are paid first out of the assets of the company. Similarly, all costs, charges and expenses of liquidation are payable out of the assets of the company prior to all other claims except those of secured creditors, if any. The same rule applies in a voluntary winding-up (Section 217).

Test and Examination Questions

On Company Law

1. Who are members of a company? How does a person become a member, and how does he cease to be one? What are his rights and liabilities?

2. What is a private company? State its importance privileges. Describe the procedure for converting a private company into a public company.

3. In what circumstances may shares be forfeited and what is the effect of forfeiture? Has a member whose shares have been forfeited any liability towards the company? How are shares surrendered?

4. Distinguish shares from stock. Explain the various classes of shares.

1. Define the term 'Managing agent'. Give the legal provisions regarding their appointment, remuneration, removal and disabilities, incorporating the provisions of the 1951 Act.

6. (a) Define 'debenture'. Discuss different kinds of debentures. Differentiate debenture with debenture stock. What remedies are available to debenture-holders for realisation of their security?

(b) Define a 'floating charge', and distinguish it from a fixed charge. When does a floating charge cease to be afloat?

7. "An auditor is a watchdog, and not a bloodhound." Discuss with special reference to his duties, powers and liabilities.

8. What are the duties and powers of a company director under the law? Explain clearly. (Agra, M. Com. 1947).

9. Discuss the law relating to the removal of and the vacation of office by a director. (Agra, B. Com. 1948).

10. Set out the main differences between a partnership firm, a private limited company and a public company? (Calcutta, B. Com. 1946).

Agra B. Com. Exam. 1951 :

11. What do you understand by Articles of Association of a company? How can they be altered or varied?

12. How may a company increase its share capital? Give clearly the procedure in this connection.

13. In what ways may the debenture of a company be redeemed? Explain clearly.

Agra B. Com. Exam. 1952 :

14. What is a 'Prospectus'? Explain how for the directors are responsible for the statements made in the Prospectus?

15. Give a brief description of the documents and statements which have to be filed with the registrar before and after the incorporation of a company.

16. How can a company go into voluntary liquidation?

Agra M. Com. Exam. 1951 :

17. Write a note on either (a) the promoters of joint stock companies, with special reference to their fiduciary relationship with the company or (b) the powers of the directors of a company.

18. In what ways may a person (a) become, (b) cease to be a member of a company? Explain the difference between the legal and equitable ownership of shares?

Agra M. Com. Exam. 1952 :

19. Distinguish between transfer and transmission of shares. What procedure is followed in each case?

20. How, and under what circumstances, can a company (a) reduce, (b) increase, and (c) reorganise its share capital?

R. A. Final Examination :

21. (a) Describe the contents of the memorandum of association in the case of a limited by shares limited by guarantee and unlimited company (1940).

(b) State the distinction between Memo and articles of association of a company. Give a full answer. (1940).

22. State the courses to be followed by the liquidator in settling the list of contributories, and say how, and upon what grounds, the lists may be varied and by whom? (1941).

23. Distinguish between the different classes of companies which may be incorporated under the Act? Also mention the circumstances in which a company may be wound up by the Court (1943).

24. State the law as set out in sec. 4 of the Indian Companies Act 1913, regarding compulsory registration of associations formed for the purpose of carrying on business. What are the legal consequences where an association, being compulsorily registerable under the Act, is not registered? (1945).

Allahabad L. L. B. Exam. :

25. What is the difference between a share certificate and a share warrant? What is the position of a share warrant holder in respect of a company which has issued it? How is the dividend paid to him? (1939)

26. Write short notes on :—

Committee of Inspection; Floating charge; Preferential payments, Guarantee Company, Statement in lieu of Prospectus. (1940).

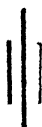
27. Who is a liquidator? When and how he may be appointed? Discuss his legal position and powers carefully. (1943).

28. (a) Explain the "doctrine of Internal Management" applicable to companies.

(b) Does a suit lie, at the instance of a shareholder, for declaration and injunction, on the ground that the directors have abused the powers to borrow and to invest the funds of the company vested in them under the Articles of Association? (Agra L. L. B. Final 1952).

BOOK TWO

Problems of Management



CONTAINING

Philosophy of Management ; The Social responsibility of management ; Management of Production; Management of Labour; Problems of Indian company management; Share-holder's Control E t c. E t c.



*Indeed, if the fundamental problem of industry can be reduced to the limits of a single question, that question would be—
“How best can we achieve and maintain a fair balance between the things of production—the machine, the buildings, the materials, the systems—and the humanity of production—the workers, the foremen, the manager, the share-holders ? This is the problem which is at the root of all the problems affecting industrial management.” —‘OLIVER SHELDON’*

CHAPTER I.

PHILOSOPHY OF MANAGEMENT

Introduction :

Management as a function of industry, is absolutely distinct from its partners—labour and capital, it remains the stable element in the interplay of both. It is not tied to capital since normally it has little or no financial interest in the business it directs. It is not attached to labour, since its function is the direction and control of labour. In its work, however, it must constantly be guided, not only by the facts of the situation, but also by its comprehension of the general as well as local mentality of its partners. Management in a large measure “is the management of men” and unless it understands the mentality of its men, it cannot be effective. The interpretation of that mentality is the preliminary task of management, and it is only by dealing with the human problems involved as primarily questions of social rights that management can hope to steer the bark of industry into peaceable waters. Industry cannot be rendered efficient, while the basic fact remains unrecognised that it is primarily humane. An industry designed to meet the needs of our life must be living. And for this, the aim of management must be to render industry more effectively human—more truly a corporate effort of human beings, united for a common object and moved by a common motive. In order to achieve that end there must firstly be a motive and an ideal; secondly, leadership and coordination; thirdly, work and cooperation. All these factors are interdependent. “The ultimate motive of industry should be that of service to the community; that the art of leadership will develop with the growth of science and the realisation of the social responsibility of management and that cooperation will come when the motive or the ideal is real and when the leadership is compelling.”

The social responsibility of management :

The responsibility of management to the community cannot be exaggerated. It is a human responsibility, occasioned rather by its control of man than its application of technique. Whether management knows much or little of its own science, its responsibility remains unaffected. Management is the representative of the industry, and, in fact the community, and is charged with the responsibility of producing those goods which are socially desirable

and to make them available to the members of the community at a fair price. This is the foundation of that theory which postulates "Service to the community" as the primary motive and fundamental basis of industry. The ideal of service, in fact, subordinates wealth, its creation and distribution to the higher necessity of wellbeing—a wellbeing not of individuals, but of all the component parts of the community.

There are in short three implications of the motive of service; firstly, that management shall value its policies and methods by ethical as well as economic standards; secondly, that it shall aim at a structure wherein each individual gives of his best and is called upon to express his personality (if not in the actual operation he carries out) at least in his relations with his fellow workers and the management; and thirdly, that it shall so conduct its business that all engaged in the industry have the opportunity to devote their highest faculties to the attainment of the ideal. Progress towards these ideals requires more highly developed management.

This is not all. "Service to the community" does not consist simply in supplying the desired goods at a fair price but it also consists in supplying the citizens it requires to enable it to advance. Management, thus, is further loaded with responsibilities which stretch beyond the local sphere of production. The employees in an industry are not solely a means for production of goods, but also an agent in social progress. An employee is not only a worker but also an individual. This is the basic principle which forms the social obligation of management—the obligation to reward the worker, not as a perquisite of industry, but as an individual loaned to the industry for the betterment of the community. The worker lives from morn to night under the environments created by the management and according to the proverb that "a man is the product of his environments" the character of management is most likely to be reflected in its workers. The influence exercised by the management upon the individual workers naturally reflects in other walks of their life also; the spirit inspired by the management in its workers, inevitably affects their spirit as parents, voters and citizens. Management is, in this sense, a good teacher which can turn out disciplined citizens. Better management can make a state great because of its citizens, homes happy because of their parents, communities high-minded because of their counsellors, or it may crush state, home

and township under the weight of an apathetic, careless, toilworn, degraded or selfish mentality among the mass of the people. Better management requires more highly developed management, bred up in democracy and education and having a sense of respect for the labour.

Management has, however, the obligation to make most of each individual not only that the service of industry as a whole may be the richest, but also that the service of each individual may be developed to the highest degree.

Good service is only possible upon a basis of efficient cooperation. The social responsibility of management is to carve out the path of cooperation in service, so that the economic service of the community may produce not only the material wealth, but spiritual well-being. When the management comes to be actuated in its everyday affairs by a motive which transcends self-interest, the moral progress of our community may be said to have begun.

Management of production :

Another fundamental of ideal management consists in the scientific management of production. To debate the necessity of increased production is unnecessary. The present day socio-economic conditions of the world demand an alround increase in production. The duty of fulfilling the call for "Produce or Perish" devolves on the shoulders of the management. But the management in its enthusiasm to discharge this duty must not forget certain important principles. Ideal management of production involves the following important considerations :—

Firstly, the right type of production is an art, and it requires a strong and able manufacturing manager which it is the duty of the management to select and appoint. The manufacturing managers "must be 'big men' not only 'big' to command but 'big' to understand, 'big' to study the science of their management, 'big' to grip and kindle the spirit of their men, 'big' to inspire by the sheer leadership of personality and by the possession of a trained understanding of all conditions and movements in the industrial world."* Thus the necessity of a strong manufacturing manager is the first essential of 'Ideal Production.'

*"The Immediate Future of Industrial Management". By Oliver Sheldon in "Business organisation and Management" (Sept., 1923).

Secondly, the production of the goods must be 'greater', 'cheaper' as also 'better'; one without the other cannot be said to constitute the maximum service to the community, which is the function of the industry. The above three terms, may be described as follows. There should be 'greater' production, which must absolutely be in accordance with the demand of the community, or there should be not deficit production in any case, but at the same time there should also not be production in excess to the demands of the community. Surplus production is the direct road to stagnation. What is, therefore, needed is 'greater' production which should be at prices within the means of the average consumer. Production should be 'cheaper', and for this it is essential that it must be accompanied by economies in production in order that the costs of production might be low to allow the prices being reduced to a level at which increased consumption is possible. Then, there should not only be quantitative but also 'qualitative' production. Volume without quality is not the best service. "More art in industrial production means more spirituality in the maker and purchaser. More scientific research into the quality of goods means higher intelligence applied in the production and the purchasing of those goods. Only if the production is of things worth producing, can a factory claim to be rendering its fullest service."* This quantitative and qualitative production is, in toto, dependent upon the combination of both the personnel and the impersonal factors or what may also be described as—the human and the material agencies. The term 'Personnel Factor' stands for a greater demand upon the individual, either by greater exertion of hand and brain or by a rearrangement of his physical methods of operation. The pioneer exponent of 'Scientific Management', Mr. F. W. Taylor, has emphasized the necessity for the scientific treatment of manufacturing problems. And the scientific treatment of production problems, in fact, implies the impersonal factors or the material agency. We really require a more analytical outlook, a scientific attitude towards the problems of production the attitude which approaches every problem from a stand point of detailed inquiry, divides the problem into its constituent parts, disentangles every maze, advances only where proof is absolute and builds upon assured foundations.

Thirdly, the efficient management of production requires the establishment of 'Research' in industry. Industrial research is a part

*"Philosophy of Management"—By Oliver Sheldon, Page 200.

and parcel of the material agency which helps to a very great extent in affecting economies in production. There are two types of research—Pure and Industrial or Applied Research. Pure research is not the concern of industry and should be carried on by the universities and other research associations. But it may be pointed out that there should be the closest cooperation between such bodies and the research workers of the industrial organisation. Industrial research is really the function of the industry. According to Mr. A. P. M. Fleming, "the requirements of a research organisation are those relating to the development of new tools, processes and methods, the elimination of difficulties arising from time to time in manufacturing operations; the data required for new designs, the establishment of means of recovery of by products, the utilisation of waste products, and similar other economic considerations. Further, a continuous check is required on the quality of raw materials supplied, and the establishment of standards of quality which will enable purchases to be made, as far as possible in the open market."* Management as a body should appreciate the services of the research workers and adopt their researches. More often than not, the management regard the research as an infringement of his legitimate province, a reflection on his capacity. This attitude must go and instead the management must learn to appreciate the aids of research—to view its inquiries and recommendation as the equivalent of costing in terms of mechanical, chemical and electrical services.

If management is a science, it must adopt definite methods to achieve ends. Just as there are formulae for chemistry so must there be formulae for management, "The chemist mixes a definite quantity of this and a definite quantity of that, and he has what he knew would be the result of the combination of the elements", says Mr. C. E. Knoepfel, "The manufacturer mixes tons of this, feet of that, so many machines, some money, men and knows absolutely nothing about the real outcome as regards cost and efficiency until the product is completed."¹ This is the revelation not only of lack of accurate and immediate knowledge, but also of lack of that type of mentality which can map out a course for its activities and proceed methodically to follow that course. It may be, therefore, suggested that every industrial organisation must also

* "Industrial Research" By A. P. M. Fleming O. B. E., M. Sc., M. I. E. E., in "Lectures on Industrial Administration." (Pitman)

1. "Industrial Efficiency Methods", By C. E. Knoepfel.

possess cost accountants who must be a part of the manufacturing department and should be directly linked with the management also. This is the fourth essential of sound production management.

Costing and Research together give birth to standardisation. Every management must realise the importance of the principle of standardisation and practise it. Mr. Harrington Emerson¹ has shown that efficiency is based upon twelve principles, of which three are concerned with standardisations—standard conditions, standard operations and written standard practice instructions. Mr. Oliver Sheldon further observes in his 'Philosophy of Management', 'if management in Taylor's definition, be 'the art of knowing exactly what is to be done', how much simplified is the task if a large proportion of it is reduced to a standard practice ' How much simplified is the production if both the character of the product and processes of manufacture are standardised so that every suggested improvement can be accurately weighted against the standard.' The definition of a standard by Mr. Morris L Cooke, conveys the best idea of the principles underlying the standardization. 'A standard under modern scientific management, he says, 'is simply a carefully thought out method of performing a function or carefully specifications covering an implement or some stores or some product. The idea of perfection is not involved in standardization. There is absolutely nothing in standardization to preclude innovation. A proposed change in the standard must be scrutinized prior to its adoption. Standardisation practised in this way is a constant invitation to experimentation and improvement.'* Standardization, moreover, is the basis of scientific control. "The less the variety in equipment", writes Mr. F. A. Parkhurst,² "the better the control and the greater efficiency." Mr Denning is quite justified when he says, "after all, why shou'd not each industry have its own standards' association like the engineers, and from time to time issue approved definitions and specifications ?

1 "Twelve Principles of Efficiency" By H. Emerson.

* From "Academic and Industrial Efficiency", Bulletin V of the Carnegie Foundation for the advancement of learning, written by Mr. Morris L. Cooke quoted by Oliver Sheldon in his "Philosophy of Management" Pages 212 and 213

2. "Applied Methods or Scientific Management", By Fredric A. Parkhurst.

The fifth sine-qua-non of an efficient production management is 'Planning.' There should be a well-laid out plan, carefully devised by the management with the assistance of the manager of the manufacturing section. It may be emphasized here that the written instruction form an important part of planning. Most of the managements do not realise the importance of 'Written Instructions.' In a majority of concerns, the higher officers specially know their duty only in a general way and do not know with any exactitude the detailed methods by which their work is to be executed. This is equally true of foremen and clerks. There is a wholesale lack of definitions, the administrative picture is a blur, not a design. This lack of definition is calculated to occasion greater in efficiency than a similar lack in the duties of the workers. Moreover, regular and constant conferences upon departmental matters (between the various heads of the manufacturing section) is another essential of good management.

Then the sixth essential is Time and Motion Study. The essential ingredient of time study is the cooperation of the worker himself. Just as mechanical research calls for an engineer, and material research calls for a chemist or metallurgist so human research calls for a psychologist. It is not, of course, necessary that every time study men should be made by a trained psychologically and be under the direction of a trained psychologist. It is not practicable to distinguish time study from motion and fatigue study. Inherent in motion study is the timing of the job. Motion study calls for the capacity of winning and interesting the worker, it calls for the qualities of sympathy, humour and understanding, it calls for a knowledge of muscular and mental reaction. It is infact the task of men trained by and working under a psychologist. Thus the time study cannot be divorced from motion study.

Management of labour :

Labour management is also an essential function of "Management", and the smoother the industrial relations (between the workers and those who control them), the better the management. The problem of labour is the 'Kashmir' front of the industry. It is a perpetual problem, a developing problem and a psychological problem. Like the problem of Kashmir in the political field, it needs not only skill, practical statesmanship and the power of constitution building, but also vision and understanding. Changes

in the hours of work, increase in wages, the establishment of Employment Exchanges, and the encouragement of welfare work may too often resemble with many of the issues of the 'Kashmir' Problems. What is required is not the schemes and departments but sympathy and insight. The fingerpost of progress points to the path of cooperation. In the following paragraphs it is proposed to analyse the spirit that is required in the main fields of labour management, ways, employment and welfare. It is difficult to condense a volume into a few paragraphs but still it has been attempted to suggest a path for the managements to follow.

Minimum wage :

The problem of wages involves the determination of that particular part of the proceeds of the industry which is payable to labour. This problem has two important aspects, social and economic, and the efficiency of management is dependent upon the fulfilment of both these aspects of the problem of wages. From the social point of view, the wages must be so fixed as to be conducive to the workers' physical and moral welfare; and from the economic point of view, the wage must be so adjusted as to be conducive to the maximum of production at the minimum of cost. In short the wages to be paid to the workers must be 'fair', the lower limit of which be the minimum wage,* and the upper limit be determined by the capacity of the industry to pay. It should also be added here that even the 'minimum wage' must be based on an assumed minimum of productivity. Wages and profits are like the two sides of a triangle, the apex of which is fixed. Production is the base of the triangle. Just as the extension or the contraction of the side of a triangle is dependent on the length of the base—if the base is short the side are contracted and if the base is long the sides are extended. Similarly, wages as also profits are conditioned to an appreciable extent by production. The workers should be told the philosophy of this triangle. Further, it may also be suggested that in the settlement of wages, there should be a tripartite agreement between the (i) Labour, (ii) Management, and (iii) Consumers or the Community in order to arrive at a sound rate. The role of the

*The term 'Minimum Wage' here represents a living wage, which provides not merely for the 'big' three essentials of life—food, clothing and shelter, but also provides for a measure of frugal comfort including education for the children, protection against illhealth, and a measure of insurance against the more important misfortunes including old age.

community in the settlement of wage-rates has never been emphasized so for Community's representation is essential because an agreement between the management and the labour might ruin the community. It is not inconceivable, the management is likely to care more for its profits—thus the interests of the community (which lie in an equitable price) are likely to be jeopardised. The state as a representative of the community can restrict the profits accruing to the capital, and at the same time can also help in the adjustment of such a wage which might not be disproportionate to the earnings of the business or industry.

Profit sharing and co-partnership :

In recent years there has been a recrudescence of enthusiasm for schemes of profit-sharing and copartnership. But not much is to be hoped so far as these schemes are concerned. Apparently, the plan appears to be sound but it does not touch the basic problem of wages. The spirit of bargaining, as is claimed, is not overcome to any appreciable extent of course in so far as the profit sharing attempts to formulate an acceptable balance between standard profits, and endeavours to distribute the surplus upon an agreed principle, it goes some way to limit the bargaining, but it does not obviate the necessity for fixing the wages according to the powers of the two parties. It is, therefore, supplementary, but not an alternative to bargaining. Neither can profit-sharing be regarded as stimulating increased productivity. The payment bears no direct relationship, as does payment by results to effort expended. Again, profit sharing is not an immediate and vivid incentive. The plan is, in toto, dependent upon the annual profits. Profit sharing is infact an arrangement where the burden of loss falls only on one section (the employers) but the profits are shared both by the management and workers. Thus the uncertainty of benefit and the remoteness of the reward tend to diminish the enthusiasm of the workers in the plan.

The general attitude of the labourers as also their leaders too is for the most part indifferent towards profit sharing. The dangers to Trade Unionism are obvious, since there might easily be an attempt through profit sharing to weaken the solidarity of labour by attaching the profit sharing employees to their own firm rather than to their organised fellow workers. There is a further danger that profits might be manipulated by setting aside of reserves etc.

So that the portion accruing to the labour would be insignificant. Again, as Mr. W. L. Hitchens points out, "there would be glaring inequalities, amounting to injustice as between one firm and another." If profit-sharing can materially contribute to the development of a sense of justice in industry its value may be immeasurable. There is again, the very real danger that profit sharing, by a union of labour and capital through their respective organisations might be made a weapon against the community.

In conclusion, it may be remarked that profit-sharing may be more advantageous in the case of large joint stock concerns. Profit-sharing to be successful, needs a religious and ethical spirit behind, which is a rare phenomenon these days. And in view of this factor the profit sharing schemes have failed all the world over. What is in fact required is a contented labour force, and incentive to produce more. And both these objectives can be achieved in a better way and more satisfactorily by better wages, better working conditions and production bonus rather than by profit-sharing.

The scheme of co-partnership does make a definite change in the status of the worker. The worker under this scheme, plays a triple role. He participates in the wages as an employee, gets dividend as a part-owner of the concern, and has also a voice in the management as a shareholder or member. It promotes industrial democracy. But the socio-economic conditions of the country in general and the workers in particular disallow the practice of such a plan. The workers are hardly able to make their both ends meet, what to say of investing in industrial securities. Moreover, they are illiterate and ignorant and do not know the rights conferred on the shareholders by company law. And so if they are allowed, under co-partnership, to participate in the management along with their trained and experienced directors, they are more likely to make a mess of the whole affairs instead of improving the quality of the decisions. Further, copartnership might be unpopular with the workmen themselves, because they do not want to be tied down to their shares.

Employment and security :

The second task on the labour side of management consists in the maintenance of an efficient labour force, which is in toto dependent upon decent conditions of employment and security.

The work of employment is essentially a necessary piece of managerial organisation, and is concerned with the engaging, transferring and discharge of workers. It may be suggested here that the employment work should be organised as a distinct department, and certain principles be strictly observed in the movement of the personnel. It is the duty of the management proper to see that employment department is well organised and is entrusted to an experienced manager.

Well, the first problem of the employment manager is the management of the right type of personnel. It is a highly specialised function and is indeed a combination of spirit and science. The Employment Manager must be extremely cautious in this respect. Prevention is better than cure. He owes a great duty to the concern, and must, therefore, select only those men who are most suited for the work according to their capacities. The instinctive discernment of the naturally able employment manager requires to be supplemented by scientific psychological tests. Such psychological analysis works in two complementary ways; firstly, by analysing types of work and determining the predominant characteristics required for the work; secondly, by analysing the qualities of the applicant by tests directed to that end, with a view to determining how far he possesses the qualities necessary for the efficient execution of the work. The gradual collection of data ultimately results in standard tests, being formulated for specific jobs.* It may further be suggested that an industrial psychologist should be regular member of every management (in the machinery of organisation) and he should assist the Employment Manager in the selection of the personnel. If by psychological tests a man is proved to be fit, he must also be medically examined in order to ensure that the present employees are exposed to no risk. The selected persons should be received in an atmosphere of welcome—they should first be introduced with the foreman, the work-mates and their work. The departmental manager should do his best to imbue the new worker with a high conception of his duties, with something of the spirit of the concern.

* Vide : Lectures on Industrial psychology—By B. Muscio. Vocational Psychology—By H. L. Hollings Worth. Mind and work—By C. S. Myers, M. A., M. D. Psychology and Industrial Efficiency—By Hugo Munsterburg.

(Extracted from 'The Philosophy of Management'—By Oliver Sheldon, Page 164).

The movement of the personnel within the factory, again, is a problem, and, requires a central organisation to effect the necessary transfers between the departments. The scientific mastery of the methods of production cannot make good the loss resulting from a disregard of the human element. The figure of 'Labour Turnover', i. e. those discharged from employment, is an index of factory human conditions. It may be suggested here that the permanence of employment for efficient workers should be the objective of all employment work. The employment department must go deep into the reasons for the movement of the personnel. It should coolly ponder over the problem as to whether poor management, lack of prospects, poor selection, bad condition, unsympathetic foremanship or unhealthy home environment is the main cause for the increased labour turn-over. After pondering over these queries, the employment manager should try to find out the reasons therefor and must then regulate his policy accordingly. The wages should be regulated in such a way as to afford an adequate and fair reward for the services of the employees. Work should be arranged in such a way that the employment might be maintained at a steady level and this is possible by providing suitable and better conditions of work. Moreover, the Manager should also welcome criticism and suggestion. He must keep an open door for complaints or any type of trouble. He must constantly present the human view point in all questions of debatable policy and inspire the heads of departments to give full weight to human considerations.

The discharge of the personnel, again, if we are to regard the worker as something more than a cog in the machine, cannot in justice be entirely left on the sweet will of the individual foreman. Sometime certain circumstances (e. g., trade cycles, seasonal fluctuation or misconduct on the part of employees) contribute to the ebb and flow of personnel, which becomes inevitable in certain cases. Justice is required in this respect. Just as in social life an individual is governed by laws of his own making and tried by juries of his peers, it may be suggested, that a similar course be followed in industry also. When the circumstances demand discharge, the reduction of the staff must be on the basis of efficiency. The most inefficient worker must go first. But, when degrees of efficiency are equal, other considerations may be followed, such as single man before married man, the man with no family or dependents before the man with family; the man with short service before the man with

long and honourable service; the man with no domestic troubles before the man who is over-burdened with them. And in all such cases the cooperation of the workers' representatives must always be sought otherwise every discharge is likely to lead to a chaos in industry.

As already observed, maintenance of an efficient labour force is dependent to an appreciable extent upon the decent conditions of security and it is suggested that the management must leave no stone unturned in order to minimise the unemployment and create a 'sense of security' in the minds of the workers. The time when it will not be possible to employ usefully the whole of our labouring population, as Sir William Beveridge says, "has not come, it is not within sight, it can be imagined." The three principal agents of production are land, labour and capital, and it is really an egregious misconception to think that there is too much labour, when, on the onehand, it is admitted that there are vast reserves of land as also capital. The problem of unemployment, as a matter of fact, is one of adjustment. The industry should be organised in such a way that labour is made available and is economically employed where ever required, and that, where periods of unemployment are inevitable, its menace disappears. And this infact is the function of management. In order to minimise the hardships incidental to unemployment, it may be suggested that there should be better and planned adjustment between the contribution made by the three principal agents of production.

Welfare work :

The third task of the labour side management consists in the provision of welfare work. There are no two opinions as regards the necessity of welfare work. Welfare work aims at assisting the individual to fulfill his function both as a citizen and producer in the interests of the community as well as of the particular enterprise with which he is attached. It seeks to smoothen the industrial relations.

There are two important conditions for the success of welfare work, the absence of which is bound to nip the real object in the bud. Firstly, there should be an universal welfare spirit, without which welfare work is nothing but fraud. If the workers, as human beings, have a right to better conditions of work, it is the moral duty of the management to provide for adequate welfare work, which

must spring out from the heart of the employers. The spirit must precede the work. No amount of legislation can create that spirit for sincere welfare provision. The management must feel the benefits of true motive and spirit of cooperation. Without a motive which is interested, welfare work is a farce. It may also be pointed out here that the spirit of welfare work cannot be concentrated in a welfare department, the welfare spirit must prevail through out the organisation.

The second condition for the success of welfare work is 'co-operation'. To seek to establish welfare without co-operation is to follow a path which will soon be shewn with debris of scheme that have failed. The workers must be convinced that the welfare work pays. It has been experienced that even without the human spirit of co-operation and motive behind the welfare work, it appeals to certain employers and they continue the welfare provision. It is infact on account of two reasons—firstly because it pays, and secondly, because it is good advertising and at least wins the first impressions of the casual observants. But it may be remembered that such appeals are opposed to the spirit of true welfare work. It does pay, but the basic motive of honesty is not nice balancing of 'pros' and 'cons'. It does influence the casual observer, just as the Pilgrims Progress may be said to have 'boomed' the name of John Bunyan; but John Bunyan's motive was not to make his name a household word for all times. The following suggestions, however, will not be out of place —

Welfare work should be regarded as integral part of the science of management. It should not be taken out of mere pity or philanthropy. "Most employers keep philanthropy and business in different compartments of their mind", says Professor Marshall. Not only in industry but it has been experienced in social life also that we are apt to command ourselves for acts of so called philanthropy when, infact, we have but done our plain duty. Such an attitude is looked upon with suspicion and even antagonism by labour union and their leaders. Moreover, this sort of feudal charity is resented by self respecting workers. It is, the moral duty of the employers and the managements to provide for the necessary amount of welfare work. It may further be added that there should be no delegation of moral responsibility. In other words, merely the appointment of a welfare officer is not sufficient. What is, infact, wanted is to organise the work of

welfare as a part of efficient organisation and management. Welfare work should be administered by a committee consisting of the representatives of management and workers. Management and the workers together should appoint the welfare officers, and the representative committee should direct his work. Without such cooperation, welfare work will fail. It is only when the management learns the golden lesson of cooperation that it will find in every field, and specially in welfare a new welcome easing its path. Last, but not the least, welfare work is concerned not only with the physical, mental and moral well-being of the workers; but it is something more than this. It deals with fatigue of mind as well as of body, with monotony of work, and the nervous effects of working conditions. It is concerned with the atmosphere, the 'tone' of the work-rooms. It combats sullenness and strife as it combats monotony and disease. It aims at good fellowship as well as good health, justice as well as cleanliness, interest as well as efficiency, comradeship as well as comfort, high character as well as high spirit. Then again, the welfare work should be educative. It should enable a man to stand on its own feet and not make him a slave to the environments. Management runs the organisation, not the whole life of the workers. Of course inside the concerns, welfare work is the function of the management; but here also they should be left to direct the work. They must learn (by such educative environment) to conduct their own canteens, to recommend their own safety devices and to inaugurate and direct their own societies and other facilities.

Sympathy towards workers' unions :

Further proper management of labour also requires a sympathetic attitude towards the workers' unions. Days are gone when the workers' unions could be easily neglected or idly condemned. Trade unions should be properly regarded by the management, and also decently guided when necessary. Management must cooperate with the progress and policies of the trade unions. "The only way to cooperation is to lay the cards on the table. Firstly, there should be full recognition of the unions—a recognition not only of its right to represent the workmen, but also its ability to assist in practical management, and to contribute its full quota to the formation of policy, and secondly, the willing and honest effort to appreciate the unions' attitude and to cultivate an intimacy with

its aims and methods. 'This leads to-understanding rather than opposition..... This may begin by recognizing in each section of the factory some union representative with whom management can cooperate, and who at all times may be regarded as the legitimate mouthpiece of the workers in that section, and the normal person with whom to discuss problems which may arise..... He should be kept in touch with managerial policy, be consulted on problematic points and be intimate with departmental statistics.'*

Cooperation the panacea :

"Without the sense of solidarity, of community, of fellowship, the fortunes of man in this world would be low and brute like", said a Scotch Philosopher. This sense of fellowship is of utmost importance and any organisation lacking this important essential is bound to experience difficulties and even disaster. Cooperation is really the panacea. But, what is, infact, required is a sincere motive to cooperate, otherwise the appeal for cooperation in industry is a voice in wilderness. Cooperation can never be effective, until and unless the motive for cooperation is accepted by the parties. The difficulty of present is that the motives are not adequately appreciated and accepted by both management as also the employees. The principal motive on the part of the management is to accelerate the profits, while, on the other hand, the motive of the worker is to increase the wages and other conditions of work. Like two parallel lines, such motives cannot coincide, neither motive as such can contribute to the common good of the parties. Distrust must be abolished. There must be mutual trust. The management should have confidence in its workers, and the employees must trust the management. No democracy can be successful without the element of trust. Both the parties—management and the workers must cast aside their fishing nets of mercenary gain, leave Galilee of self interest and proceed upon the stony pathway after common goal. Industry at present, requires a motive which must be stronger than the motive of self-interest, though embracing it; it must be of general application omitting neither the management nor the workers. And it is

* "The Philosophy of Management"—By Oliver Sheldon, Pages 191 and 192.

not difficult to attain this ideal. The management must realise and appreciate this view point. The expression "Workers sharing in the management" should not be misunderstood. It does not stand for co-partnership absolutely. "Sharing in Management" simply means that all problems, involving difference of opinion between the management and the workers should be settled in cooperation with the workers or their representatives. Works councils or committees can be utilised for this purpose.

If management is to stand for this new motive, the manager of the future must be of a new fibre. He must be less of a technician and more of a "Captain", less of a "Boss" and more of a leader. Cooperation will come not by management sharing in the work but by the workers sharing in the management. Only in sharing it, will the labour find its opportunity to forget the dissensions of the past and to mould the factory consciousness into a living corporate spirit of brotherhood.

CHAPTER II

SHAREHOLDERS' CONTROL OVER COMPANY AFFAIRS

Introduction :

A joint stock company is sometimes defined as a glorified partnership. It is a case of skill and labour hiring capital and not capital hiring them. The most significant feature of a joint stock organisation is that those who provide the capital do not usually manage its affairs. Usually the shareholders are many and scattered over long distances. They do not possess any knowledge of business and as such cannot be expected to take any concerted action. They, therefore, delegate the management of the business to others, known as directors. Thus the directors (along with managing agent,) are the pivot of the joint stock company system. And so long as the affairs of the company are a bright and the share-holders go on getting dividend warrants regularly, they are contented ; it is only when things begin to go wrong that shareholders are prone to be critical. Individually they do not possess any power of control over the management, but collectively they may exercise such control in the following ways :—

2 Appointment and Removal of management :—

The usual form of company management in this country is in the nature of a dyarchy, it consists of directors and managing agents. Therefore, if the shareholders can control the appointment of directors and managing agents, they can, to an appreciable extent, exercise supervision over its affairs. A peep into the statutory powers of shareholders and the legal provisions relating to directors and managing agents, will bring to light certain important problems.

(a) Directors :

The principal object underlying the appointment of directors is to ensure proper control and supervision over the management by the Managing Agents. But such control and supervision have proved ineffective because shareholders do not possess real voice in the appointment of directors.

As is well known, appointment of the first directors is made by the shareholders at the time of incorporation of which the

shareholders have no voice. According to sec. 83-B (1), the signatories to the Memo. are the first directors of a company. These first directors are selected by the company promoters who are invariably the Managing agents or Managing Directors. It may be pointed out here that the shareholders, who are the backbone of any company, cannot possibly have any hold in the selection of these preliminary personalities, because they (shareholders) come on the scene afterwards. And so, in practice, it is the promoter who rules the appointment absolutely.

It is no doubt true that under sec. 83-B (2/3) of the total number of directors are liable to retirement in rotation ; but the 2/3 rd quota is not limited to persons unconnected with the Managing agent in point of interest, relationship, business or otherwise. This is a grave defect of which full advantage has been taken. A study of prospectuses discloses that the 2/3 quota has often been made up of vendors, partners, co-shares, relations, brokers, solicitors, etc. of the Managing Agent or Managing Director as the case may be. It is also significant that one and the same person often figures in directorates of various companies in the same group. Moreover, it is easier to upset a ministry than a Board of directors, because the provisions of sec. 83-B (2) sound well in theory only ; in actual practice they evaporate in thin air. The power provided by the above section is but a paper-right and the election of directors is a mere farce. In practice, the vacancies on the Board are filled by co-option, and the members are not in a position to put those whom they want, since the majority of votes are monopolised by the wire-pullers—the promoters, Managing agents and their friends and relations. According to S 871, one third of the whole number of directors are to be appointed by the managing agents. Besides this, certain seats are reserved for special interests. Whatever remains is a nominal number, and that too is controlled by the Management and their friends and relations. The true situation is this. Directors are supposed to be elected by shareholders, but the fact is quite different. The shareholders lag behind at company meetings. They do not, in fact, control the majority of votes, and hence have no say at all. They, being scattered and disorganised, scarcely dispute the nominations. Being mostly illiterate, they are unaware of their own rights, what to say of other provisions of the Company Law. They are also never careful to attend the company meetings. They

care a fig as long as they go on getting regular dividend warrants and are stirred only when it is stopped or when there is an appreciable diminution of it. Again, the Articles of Association of most of the companies contain a provision to the effect that the office of a director would be ipso facto vacated, if he is asked by the other co directors to resign. Some of the articles even go to the extent that a director would ipso facto vacate, if in the opinion of majority of directors, he is doing anything which may be considered harmful to the company. Thus if per chance the shareholders at any time succeed in putting on the Board any director of their choice, he could be unseated at the behest of the other directors or a majority of the directors.

Further, in the filling up of casual vacancies and making of additional appointments, the same tendency is evident. Thus, in the appointment of first directors as also in filling up of vacancies and appointment of additional directors, the shareholders have no voice whatever. The only occasion when they have any voice is at the time when the directors retire at Annual General Meetings. But here also the practical difficulties with which they are faced are so great that it is hardly possible for them to exercise their right effectively. In the first place, the Articles usually provide for a certain number of day's notice to be given to the company, if a person other than the retiring director is to be proposed. It is a great hindrance. Coming to the other difficulties, it would be obvious that if it is decided to appoint a new director in place of the retiring director, it is essential to canvass proxies and obtain for that purpose the list of shareholders. The transfer books are generally closed at the time of the annual general meeting and the proxies are to be lodged 72 hours prior to the holding of the meeting. Considering the time involved in obtaining the list, preparing circular and proxy forms, getting them printed and posted to shareholders scattered all over the country, getting them back by post, checking them, noting them, listing them and ultimately depositing them in the company's office, it is obvious that the shareholders have no time left to make the necessary preparations, and it is practically impossible for them to organise concerted action in order to exercise their corporate right of appointing new directors in place of the retiring ones. On the other hand, the Agents and Directors possess the list of shareholders with them and are free to canvass proxies well in advance of the meeting. They

also make the fullest use of the company's secretariat and are entitled to canvass proxies at the company expense. Thus, if the Managing Agents and Directors can whip up 25 to 30% of the total voting power—and this is very easy for them, the shareholders can be successfully kept at an arm's length. The cumulative effect of these hurdles, handicaps and difficulties are tremendous. The shareholders feel that they are in an unequal fight as the whole system of election from beginning to end is one sided. They feel that the dice is loaded against them and, therefore, they seldom think of opposing the retiring directors, although they can do so on a fair field.

As regards the removal of directors, section 86-G provides that the members of a company may, by an extra-ordinary resolution remove any director whose period of office is liable to determination at any time by retirement of directors by rotation, before the expiry of his period of office and may by ordinary resolution appoint another person in his stead, who will retire at the same time as the person whose place he has taken. Under common law, however, the members may remove a director on account of pecuniary misconduct, negligence, incompetance and permanent disability. The point to be noted is that here also the powers of shareholders are very limited. The ex-officio and special directors, who are mainly responsible for the administration of the company are not subject to removal by the shareholders under sec. 86-G. The debenture-directors too, who are in most of the cases members of the managing agency firm or all otherwise connected with them, are equally immune. As regards ordinary directors, they also cannot be easily removed against the wishes of the management, because if the shareholders want to do so, they must possess the majority of votes. It is well-known that the managing agents and directors generally possess—and where they do not possess, they easily make up—the required voting strength in order to defeat the object of members*.

(b) Managing Agents :

Under sections 87-B and 87-BB, the appointment, removal or changes in the agreement of managing agents are not to be valid unless approved by the company in general meeting as also by the Central Government ; but a preliminary appointment announced in the prospectus or statement in lieu of prospectus is saved from

* Business Organisation by P. R. Gupta Page 125-

this restriction. From this it is clear that the shareholders have absolutely no voice in the appointment of the managing agents of a company.

As regards the removal of managing agents, section 87-B (a) provides that they can be removed by shareholders by an ordinary resolution passed at a general meeting, if they are guilty for a non-bailable offence relating to the affairs of a company. Again, in the absence of contrary provisions in the articles or the agency-agreements, they can also be removed under common law by shareholders on the grounds of pecuniary misconduct, negligence, incompetance and permanent disability. Besides the bar of contrary provisions in the articles, there is one more difficulty, that if the managing agents are removed by shareholders before the expiry of their term of office, compensation is usually payable to them in accordance with their agreement. This is definitely a serious obstacle in the way of their removal.

2. Appointment of Auditors :—

The first auditors of a company are appointed by the directors prior to the statutory meeting; and the subsequent appointments are made annually at the general meetings. It must, however, be noted here that the shareholders have no say in the appointment of the first auditors, and they are also unable to put their representatives at the annual meetings because they do not possess the necessary voting power.

3. Periodical Report and Accounts :—

According to sec 77, every public company limited by shares and every public company limited by guarantee and having a share capital, must hold a general meeting of its members within a period of not less than a month nor more than six months from the date on which it is allowed to commence business. The principal object of this statutory meeting is to give the shareholders an opportunity of knowing at an early stage the details of the formation of the company, to what extent the financial appeal has been successful and what has been done with the actual money received in payment of shares. The statutory meeting enables the shareholders to discuss these and any other matters arising therefrom.

Further, under section 76, a general meeting of every company must be held within 18 months from the date of its incorporation, and thereafter once at least in every calendar year. At these

annual greetings, the final accounts, a copy of which is circulated to each member 14 days before the date of the meeting, are adopted by them. The accounts (consisting of the P. & L. a/c and the Balance Sheet) and the Directors' Report supplied to the members contain sufficient material about the upto-date state of affairs of each company. The object behind this provision is that the members might be in a position to know the exact position of their company and might review the work of their agents. If they are dissatisfied, they are at liberty to criticise the accounts etc. at the meetings. Usually "question time" is given to the shareholders at all general meetings by the chairman, and it is then that they may not only ask questions but also ventilate their views as to the manner in which the company is directed, and make suggestions for the consideration of the management. And, if thoroughly dissatisfied, they are entitled even to reject the accounts out right and appoint a committee of shareholders to inspect the books of account and vouchers of the company and to make a report to the members of the company at an adjourned meeting. But this method can be of any practical utility only where the directors themselves have nothing to hide and are in sympathy with the committee, because there is no power given to such committee to examine witness on oath.

4 Appointment of Inspectors : —

Section 138 provides a means of investigation by inspectors who are appointed by the state governments to carry out an investigation on behalf of share-holders on the application of members holding a specified proportion of the issued share capital, such proportion being $\frac{1}{5}$ in the case of banking companies and $\frac{1}{10}$ in the case of other companies having a share capital. In the case of a company not having a share capital, such application may be made by not less than $\frac{1}{5}$ in number of the persons who are on the company's register of members. This is the strongest weapon in the hands of shareholders, because by it the part and present directors, officers and agents of the company may be made to produce to the inspectors all books and documents in their custody or power, and may be examined even on oath in relation to the business of the company.

Another statutory method of investigation is provided by sec. 142, under which the shareholders may appoint the inspectors without having recourse to the state government. They will report

to the members by whom they are appointed and they possess the same powers as the official inspectors.

5. Complaint to Registrar :—

Under section 137 (6), if it is represented to the registrar in materials placed before him by any shareholder that the business of the company is carried on in fraud of persons dealing with the company or for a fraudulent purpose, he may after giving the company an opportunity of being heard by written order call on the company for information or explanation on matters specified in the order within a specified time. If upon investigation the registrar is satisfied that any representation on which he has taken action is frivolous or vexatious, he shall make an investigation and submit the report to the State Government. Further, under sec. 141-A, the State Government in proper cases has to take upon itself the duty, at the cost of the State, of launching prosecution of persons who may be believed to be guilty of an offence in relation to the company. If after making proper inquiry, the Registrar is of the opinion that the complaint is false, he will disclose the identity of the complainant to the company, and the company may take legal proceedings against him for the recovery of damages.

6. Other Powers :—

Although according to compulsory regulation 71 of Table A, the powers of management of a company's affairs are vested in the directors, yet there are certain matters which can be done only by the shareholders in general meeting by passing an appropriate resolution viz :—the alteration of capital ; the alteration of articles, sale of the company's undertaking, the schemes of financial reorganisation etc, etc.

In conclusion it should be noted, that barring a complaint to the registrar (which may be made even by a single shareholder) everything, else depends upon the members' commanding a majority of votes at general meetings at which any particular action is proposed to be taken by them. In actual practice, however, the shareholders seldom succeed in securing the majority of votes for reasons already stated above. Where, however, the shareholders of a company take an intelligent interest in the affairs of a company and can combine for a fight with the management, they can certainly succeed*.

* Business Organisation by Prof, R. R. Gupta, Page 127-129.

CHAPTER III.

PROBLEMS OF COMPANY-MANAGEMENT

Concentration of economic power :

One of the gravest defect of Indian Company management is the interlocking of directorate. The tendency is to monopolise the directorial control and supervision in the hands of a few persons closely conneted with executive management. The capitalist propaganda of the democratic ownership of capital is far from truth. The managing agents in India possess under a large number of concerns and of a variety of nature. A group of managing agents control about 500 industrial concerns with capital of nearly Rs. 150/- crores, and covering every field of industrial activity. This concerntration of control is common to all industries. In Jute, 53 mills (capital 23 crores) in the country are controlled by 17 managing agents. Four of them control 30 mills. Of 247 coal companies (capital Rs. 10,45,00,000), 60 companies (capital Rs. 6,38,00,000) are controlled by 18 firms, four of them controlling 31 companies. In Tea, 117 companies controlled by 17 firms, five of which control 74 tea companies. Similarly concentration of control exists with incidental variations in sugar, engineering and other industries. Even in the Cotton textile industry, a third of it is in the hands of 15 firms. In cement and Matches, virtual monopolies have been established through unified control or ownership of the industries. The biggest tragedy is that the control of industries is not only in the grip of a few managing agency trusts, but also in the hands of a few individuals. This concentration of control is specially because of interlocutory directorships—the various trusts and companies are inter—linked by a group of common directors. In coal out of 66 companies. 57 ccpanies with 247 directorships are controlled by 28 persons, seven of whom hold 64 directorships. In tea industry, 430 directorships are distributed among 40 individua's, five of whom hold 138 directorships. In jute 267 directorships are in the hands of 130 persons, four of whom ho'd 82 directorships. It is all like this : X becomes director in the group of companies managed by Y and Y becomes director in the group of X—in addition to their being director in their own groups. Thus the 'Courtesy' is being reciprocated. In fact there are only

20 men at the top who are controlling the entire corporate activity in India.*

Multiple directorships :

In India only a few persons are directors on the Boards of far too many companies. The evil of these multiple directorships or pluralism is that such directors are unable to perform their duties properly or become indifferent about doing so. This pluralism among directors is, indeed, the product of the managing agency system. The Bhabha Committee Report states that now-a-days a holding of 15 to 20 directorships by one person is common, while a holding of 30 or more directorships is by no means unusual.

It shall not be out of place to mention in this connection the views of Dr. Miss Shanta Panandikar on the subject of pluralism, She writes as below* :—

“It is generally believed that, even if a person possesses wide business experience, ability and energy, he cannot satisfactorily perform his duties as a director of 25, 20 or even 15 companies.... . Men being different, while even three or four directorships may be too many for one, 20 may not be so to another. Again, directorships of several cinema companies would be less arduous than that of a single big company, such as the Tata Iron and Steel company, the Associated Cement Company, or the Scindia Steam Navigation Company. Similarly, directorships of a few subsidiary companies may be less burdensome than those of the holding company. Moreover a person possessing broad outlook, deep business knowledge and wide experience of men and matters would prove very valuable as a director to the Boards of a number of companies, in laying down farsighted and progressive policies. Further, such a director may be able to bring additional business to the companies on account of his extensive business connections. Finally, a legal or financial luminary may be able to enrich his own knowledge and experience by serving as a director of diverse companies and at the same time benefit the companies with his enlarged knowledge and experience..... . Apart from these considerations, it may be pointed out that, as managing agents manage a majority of the companies in India, the duties of a director in India are less burdensome than those of a director of a

* “Who owns India”—Ashok Mehta.

* Commerce, dated 11 Oct., 1952.

company in Britain or in the U. S. A., having no such intermediate organisation. Moreover as long as the scarcity of first-rate industrial leaders continues in India, any legal restriction on the pluralism of directors may do more harm than good."

Depreciation and reserve policies unsound :

In another article on "Problems of Management of Indian Joint Stock Companies", appearing in the commerce, dated 18th Oct., 1952, Dr. Miss Shanta Panandikar writes as below :—

"Unfortunately, in the case of many companies in India, frequently provision for depreciation is not made on merits, that is, according to the value of the gross block, its estimated working life, possibilities of its obsolescence due to progress in scientific inventions and changes in technique, estimated scrap value and additional strain imposed upon it by double or treble-shift working, but is made on extraneous considerations, such as the amount of profits secured during a year, the remuneration of the managing agents and the dividends expected by the shareholders. The managing agents and directors of many companies try to justify the remuneration paid to them by declaring substantial dividends even in lean year..... Moreover, the managing agents, in a majority of cases, receive a percentage of net profits as their remuneration. This means that, if the net profits are substantially reduced on accounts of proper provisions for depreciation, the remuneration of the managing agents also gets reduced. The higher the provision for depreciation, the lower is their remuneration. Further some managing agents may not be interested in the long term welfare of the companies managed by them Hence, the provision made for depreciation changes from year to year according to the aforesaid considerations." Further, "since the Second World War, many companies in India have carried out capitalisation of a substantial part of their reserves generally by the issue of bonus shares and, in a few cases, by making existing partly-paid shares fully-paid, by using the reserves for paying the remaining calls."

Dividend policies lack stability :

In the third article on the same subject, appearing in the "Commerce" dated 1st November, 1952, Dr. Miss Shanta Panandikar criticises the dividend policies in the following words* :—

* For further details, please see commerce dated 1-11-52, Pages 292

"A study of the balance-sheets and directors' reports of a large number of companies for several years shows that the managements of many companies in India have not cared to pursue an even policy of trying to keep the dividend-rate stable as far as practicable. They have not built up a dividend equalisation fund and have been distributing as dividends what earnings have remained after making minimum appropriations to reserves and other funds, regard as absolutely necessary. The result has been that the dividends declared by them have been substantial or even high in boom year, but low or even nil in lean years..... The real reasons seem to be that some of the directors and managing agents are of a speculative bent of mind and prefer fluctuating to steady dividends. Some of the managements have not even cared to build up working capital out of the very large earnings of boom years, so as to be able to avoid short-term borrowing for this purpose."

CHAPTER IV.

REORIENTATION OF INDIAN COMPANY LAW INCORPORATION AND AUDIT

The necessity for reform of the Indian Company Law has been felt in this country for some time. The Indian Companies Act was last revised in 1936 when extensive changes were introduced especially with regard to the Managing Agency System. Thereafter various suggestions for further changes continued to be received from time to time, but it was decided that the new provision should be worked for a reasonably long time before undertaking any further modification in the general scheme of the Act. The reform, now, is overdue because the provisions introduced in 1936 have worked for more than thirteen years. Moreover, rapid growth of joint stock enterprises has taken place during and after the Second World War. The establishment of an Independent Sovereign Republic has further opened new avenues for them. These politico-economic changes make the reform in the sphere of company legislation all the more necessary. How to make a democracy—which company share ownership is legally held to be—really function under present conditions of diffused proprietorship is the chief basis of reform. The English Companies Act (on which is based the general pattern of Indian Company Law) has also undergone a number of changes as a result of the recommendations of the Cohen Committee. Time has now come for taking fresh stock of the situation in the light of the politico-economic developments that have occurred, and to find out what modifications are necessary in the Indian Company Law in order to encourage a healthy development of joint stock enterprise in this country and create conditions of confidence in the minds of the investors by safeguarding the interests of the shareholders.

The Government of India too was not unaware of the foibles in the Act but it would hardly take any effective step because of its pre-occupation with problems of graver importance to the community. The Government, however, appointed Mr. Tricumdas Dwarkadas and Mr. V. K. Thiruvankata Chari to examine the legislation and recommend measures to ensure orderly and vigorous growth of joint stock enterprises. The recommendations made by them have been examined by the Government of India with the help of Mr. N. K. Majumdar, formerly Registrar of Joint Stock

Companies, Bengal, and tentative proposals have been made for the amendment of certain important provisions of the Indian Companies Act, by the Ministry of Commerce. Very recently, the Company Law Committee presided over by Shri C. H. Bhabha has also concluded its work.

But this is all what the Government has done or are doing. There are still patches to be filled up. It is, therefore, proposed to discuss here the desirable changes in the sphere of company legislation (more especially with regard to their management and organisation) which must immediately be incorporated in the new Act to ensure a healthy development of joint stock enterprises.

For a planned systematic and co-ordinated development of joint stock enterprises, it is vitally essential that the state should take powers to license the starting of new and the expansion of existing enterprises. The existing law with regard to the incorporation of a company should be tightened up considerably. For the successful working of the licensing system it may be suggested that the Central Government should appoint a Controller of Companies. This Controller might be named as the Superintendent of Commerce or the Registrar General of Companies and he should be appointed on the recommendations of the Planning Department.* In making any such appointment the Central Government should take into consideration that the person to be appointed has had experience in economic, commercial, industrial and financial matters. The Controller of Commerce should act with the help of the committee representing the various interests of industrialists and businessmen, trade unions, economists and also Government. These members should be elected every third year by the different groups represented. The scope for administrative discretion and corruption is so high, that unless the Controller of Commerce is given some basic principles of incorporation and criteria for steady guidance, public confidence in the integrity of the system would be greatly undermined. And hence, besides the legal requirements with regard to management, minimum subscription, capital structure, audit etc., the Planning Department of the Central Government should lay down definite rules and conditions (*viz.* some general economic criteria, socio-

*It is anticipated that the Government will have a Permanent Planning Department

economic criteria and politico-economic criteria) which should guide the decisions of the committee of the Superintendent of Commerce.

Then, secondly, the 'Control of Capital Issues Ordinance' should be made a permanent feature, and its provisions be enacted in the Company Law. While issuing the certificate of incorporation the Registrar General should see that all the new provisions relating to Capital Issues are complied with. Every application for incorporation be required to be submitted to the Regional Registrar of Companies and the certificate of incorporation be granted by him after a favourable approval by the Controller of Commerce.

Audit. Audit is the only real protection available to the shareholders against bad management. In theory, the auditors are supposed to be the watch-dogs of the shareholders elected by them at general meetings. But the general meetings are in most cases an empty farce. The wide geographical and economic distribution of company shareholdings and their distribution among an increasing number of small holders, afford a distinct advantage to the management to get the things according to their wishes either by reason of the majority shares carrying voting rights and/or the proxies which remain ready to be used to silence any obnoxious shareholders who want to vote against the interests of the management. An auditor, therefore, remains a puppet in the hand of the management, because his appointment or removal is dependent upon the whims of the management. Consequently, if they displace the management or intend to report against it, they stand to lose their job. The managing agency system further accelerates the evil by extending its patronage to the auditors in a number of other ways such as by appointing them also as the auditors of other companies and businesses and thus making them depend on the good-will of the managing agents for the continuance of their office. "The result is that, human nature being what it is, even an honest auditor becomes obliged to continue to wink at such questionable practices as window-dressing methods, secret appropriations, temporary defalcations, etc., adopted by those in management..... The slightest assertion of independence on the part of the auditors of a company will deprive them of any hope of being continued in their job for the succeeding years."

A subsidiary evil in connection with the present system of audit is that, whenever any questionable conduct on the part of the management arises in relation to the accounts of a company, the auditors with the object of screening the managing agents have developed a nefarious practice of certifying the balance-sheet and profit and loss account with a laconic reservation such as "subject to the special report of even date." While reference is thus made to a special report, such report is not annexed to the balance sheet or profit and loss account and is studiously withheld from the shareholders, with the result that it does not come to their knowledge at all. This practice is a strategy adopted for saving the skin of those responsible for managing a company's affairs, including the directors, and, at the same time, protecting the auditors from the charges of false certification."* In order, therefore, to protect the interests of the shareholders, the provisions with regard to the auditors be suitably amended in the light of the following suggestions.

As regards the appointment of the auditors it is suggested that the first auditors may be selected by the Board of Directors for the audit of the Statutory Report compulsorily required under Section 77 of the Indian Companies Act. The subsequent auditors be appointed by the company in general meetings; but, the procedure of appointment be carefully overhauled. The writer here disagrees with the recommendations made by the sub-committee of the Indian Accountancy Board that "in the resolution for appointing auditors, the directors and managing agents shall not vote." Such a prohibition is against the very spirit of democracy. When those who are also in the management vote for an auditor, they stand as shareholders; and when such a voting, in a natural course, is obstructed, it is bound to create all sorts of complications. Then the appointment of an auditor by the Government also is not agreed. An auditor is to act as the shareholders' watch-dog, and it is only the shareholders (and none else) who can choose the best persons. The making of auditing a public activity means the denial of a say to the owners of the company in the matter of appointment of auditors. The greatest danger of this scheme is that the auditor would have no obligation whatever either to any company or any of its officers.

*Amending Indian Companies Act II by A. Ramaiya, Commerce, dated 4 April, 1950, page 577.

He shall be an independent monarch of his own wishes, free to embark upon the strictest audit possible. Moreover, such a system is likely to result in lowering efficiency (which is a well-known foible in the case of all government employees) and affect adversely the private practice system. If the system is nationalised, the motivation will be injured and the auditors will not take as much interest as they take under the private practice system because of maintaining the good name. And the constant spur of private profit also keeps up efficiency and lends a certain vitality to the system. It cannot be denied that many of the improvements in the law and accounts of companies have been due to the work of auditors themselves. Nationalisation also poses the problem about the existing auditors as it might create unemployment amongst auditors.

It is, therefore, apparent that the best course for the present is to ensure the independence of auditors without nationalising them, by depriving the directors or other officers of the company of their right to partake in the election of the auditors.

All the shareholders, therefore, (without any discrimination) should elect auditors and the only method to make it possible is to substitute the present system of election at the annual general meeting by a postal voting device. The method of electing an auditor should be modelled on the lines of election of the members of the University Senate by registered graduates. The voting papers must be sent to each and every member of the company containing the names of the proposed candidate seeking election for the post of auditors, at least one month prior to the holding of the annual general meeting, subject to their return by the date of the meeting.

The decision of the general meeting arrived through postal voting should not be deemed as final. It should further be subject to sanction by the Controller of Commerce. The recommendation may, however, be finally decided by the company at the annual general meeting. The Controller of Commerce should give his sanction on certain considerations (which if not satisfied, the appointment may be made by the Controller himself), viz., (1) that the auditor is properly qualified; (2) that he is not a local person so far as possible; (3) that he is not already extremely busy, and can conveniently discharge his functions; (4) that he is elected for the audit of a concern with the working of which he has had

experience and in which he is dealing; and (5) that the closing period of the concern is quite convenient to him.

The following suggestions made by the government should also be noted .—

(1) Provision be made for at least one month's notice to the members of changing the existing auditors.

(2) The accounts of a private company should be audited by a qualified auditor.

(3) The branch accounts of every company must be examined and certified by a qualified auditor, and if he is different from the auditor auditing the balance-sheet of the company, the latter may accept the certificate given by the local auditor or auditors. The auditor performing the statutory audit may insist on auditing personally the books and accounts of at least ten per cent of the branches of the company, and his remuneration and other charges must be paid by the company for such audit.

(4) The auditor should be the sole judge as to what is necessary for the performance of his duties, in so far as he calls for information and explanation for the purpose of such duty.

(5) The auditor should have the right to receive all notices and other communications relating to general meeting which any member of the company is entitled to receive. They should have the right to attend all such meetings and not the annual general meeting only, as at present. They should also be entitled to be heard at such general meetings on any part of the business of the meetings, which concerns the auditors.

Reform in managing agency system :

More often than not the subject of Managing Agents has been criticised by various individuals and associations and the predominating viewpoint is to mend and not to end the system. On this controversial subject the Company Law Committee very recently reported that, notwithstanding the many abuses and malpractices which have disfigured the working of this system in the present state of industrial organisation, it may still be, on balance, an advantage to continue to rely on it. For shorn of these abuses and malpractices, the system may yet prove to be a potent instrument for tanning the springs of private enterprise. The Committee.

therefore, recommended strict control to remove these current abuses and reduce the malpractices to the minimum.

The best course, however, lies in between these two extreme viewpoints. Taking into consideration all the circumstances, the total abolition of managing agency system is not advisable under the present economic structure of the country. Undoubtedly, the managing agency system is responsible to a considerable extent for the present concentration of economic power in India, but the overall situation in this regard does not give any cause for serious apprehensions. Mr. R. G. Bajpai, in his analysis on the 'Concentration Of Economic Power In India'* observes that on the basis of the figures published in the First Report of the National Income Committee, only 47.5% of the national dividend is claimed by agriculture, which is the largest slice carved out of the national cake, the enjoyment of which is widely dispersed in the country. And the net output per person engaged in the industrialist cum capitalist classes (viz., persons engaged in mining, factory establishments, banking, insurance and other commerce and transport) collectively as well as individually is Rs. 2 and 1.6 thousands per annum, whose difference with the average is not more than the proportion of 1 : 4, which denotes that there is no marked disparity in the distribution of national income; hence no heavy concentration of economic power. Although the observations of Mr. Bajpai are not in toto accurate, but it may be concluded there from that the danger signal has not yet been put up. The widening gulf between the lines of equal and actual distribution (although not represented as it actually is) is, as a matter of fact, most alarming. Any more sparing of the rod is bound to spoil and corrupt the managing agency system. Hence, very strong steps are required to be taken to stop the abuses in the system.

The overwhelming illiteracy of the Indian people more especially in the field of business organisation and management, is a serious hindrance to doing away with the institution of managing agency altogether. A successful democracy, with few intermediaries, requires literate people and trained administrators and this is the *sine qua non* of good management. The conditions in India are not satisfactory in this regard. The majority of the people (and

* "Concentration Of Economic Power in India" By Sri R. G. Bajpai, in *Indian—Journal Of Economics* January 1952, pages 320 and 321.

the shareholders are a part and parcel of that majority) are illiterate and cannot distinguish between right and wrong, or just and unjust. They hardly possess the talent to select the right people to form an efficient democracy. The results of recent elections are a witness to this fact. Further, there is an utter dearth of institutions providing courses of training in business management. Hence, the country has to rely somehow on its limited talents.

LORENZ GRAPH SHOWING DISTRIBUTION OF NATIONAL INCOME

, 1948—49.

Percentage of National Income. Percentage of persons, groupwise,
engaged in producing the Na-
tional Income.

47.5	68.2
54.8	71.1
64.7	82.3
67.4	83.2
84.1	90.4
87.8	94.2
93.1	97.7
94.8	100.0
100.0	100.0

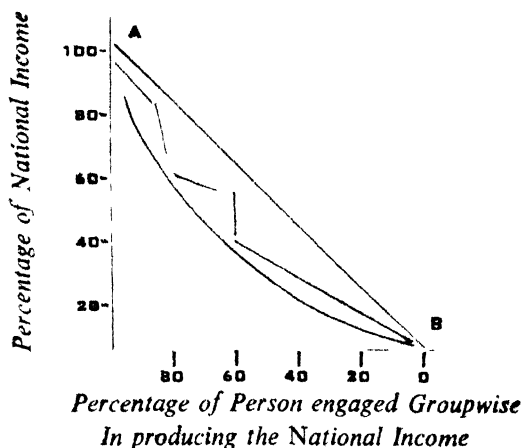
Note · Figures calculated on the basis of the First Report of National Income Committee, April, 1951.

In the graph, printed on p. 197, AB is the line of equal distribution and curve 'a' is the line of actual distribution. The distance between AB and 'a' is not large, indicating the homogeneity in the distribution of national income or lack of marked dispersion.

Then again in India, finance continues to be proverbially shy. During the last few years, Industrial Finance Corporations have been set up at the Centre and in some of the States. But the resources are very meagre and they provide loans only to the extent of about 60% of the value of the fixed assets. The financial assistance granted by the Corporation is very meagre in view of the country's demand. The companies in general are not attracted towards the I. F. C. This detraction is principally due to the

lengthy process and delays in the sanctioning of the loans, as is also indirectly admitted by the Corporation in its report.* Governmental aid to industries in the States has also not been found to be of much assistance for the purpose.

Further, the present economic conditions of the country are also anti-total abolition. The partition of the country into two units—India and Pakistan—has totally disturbed our economic



equilibrium. The agricultural industry has been ruined considerably as a result of partition. And World War II has crippled the industrial sector. Now, the renaissance of Indian economy will require the services of the intelligentsia of the country. And there is still a dearth of technical experts and seasoned administrators in India. Therefore, even if the system of management by the managing agents is abolished, those who constitute the managing agency firms will undoubtedly remain the captains of industry; and the country will have to look to them for industrial guidance and leadership. Industries which require sufficient pioneering and initial research and in which finance is not likely to be forthcoming, still wait for leadership by managing agents.

In conclusion, therefore, recommendations may be made for (a) discriminating Managing Agency system, and (b) a very strict

* "There is no doubt a big gap between the amounts of loans sanctioned and the loans availed of. To a large extent this is inevitable because it generally takes some time after sanction for the negotiations to be completed and the document drawn up and executed."—Industrial Finance Corporation Report, page 7.

control over the abuses of the system. The first part of this recommendation means that the system of management through managing agents may not be abolished *in toto* immediately but it should be retained for certain companies and abolished in others. It shall not be out of place to refer in this connection to the cogent reasons for the abolition of the managing agencies in insurances and banking business in 1938 and 1949 respectively. The most potent reason was that the function of management in these businesses is more or less of a routine nature. No great pioneering or preliminary investigation is required in these cases. Moreover, there is also no problem of finance. These institutional investors, as a matter of fact, are the cash boxes of the public, where at least the broad-minded literate people must deposit their earnings and or savings. They are the managers which must attract capital.

Further another reason for the abolition of managing agents from these businesses was to put an end to the evil practice of interlockings of banks and insurance finance. Prior to the above said amendments, different dates were chosen for the final accounts of banks and insurance companies under one management, and fictitious assets were shown in their respective balance sheets on lines of 'bond washing' in evasion of income tax. The Insurance Companies' Act 1938 and the Banking Companies Act 1949 have eradicated this evil from the fields of institutional investors. The managing agents invested valuable funds in undertakings controlled and supported by them at the cost of the poor policy-holders and depositors. Claims were not met in time and the protection afforded by banks and insurance companies was not a protection *de facto*. It may also be mentioned that a belated payment is generally a payment refused; more especially so in life insurance. The managing agency system was, therefore, uprooted to end these evil practices.

Although in the beginning there was a great hue and cry by the managing agents, time has proved that the abolition has been in the interests of insurance and banking development in this country. On the same ground the principle of discrimination should be followed in the retention of the managing agency system. The Superintendent or the Controller of Commerce should be vested with the authority to use his discretion whether or not managing agency be allowed in a particular case. Still there are a large number of companies which can do without the managing

agents, and the system must, in the interest of the country, be abolished from them. The most important of such concerns are the investment trusts and finance corporations, electric companies, key industries etc. In an elementary work of the nature it is difficult to divide the Indian industries into groups, wherein managing agency may and may not be allowed. This difficulty is principally due to the unbalanced industrial development of the country. Generally speaking, electric supply companies do not require managing agency system, as they do not involve any special problem; the work is more or less of a routine nature and trade cycles can little affect them; but if any managing agent endeavours to promote such a concern in any undeveloped part of the country, say Rajasthan, the managing agency system may be permitted there as, otherwise, it will mar the industrial progress of the country. So it should be left to the Superintendent of Commerce, who should exercise his discretion according to the circumstances of each industry. The second suggestion for the ruthless elimination of abuses in the managing agency system is self-explanatory and so no further comments on it are called for.

CHAPTER V

BHABHA COMMITTEE'S REPORT

Introduction :

The Company Law Committee, with Mr. C. H. Bhabha as chairman and 11 other members was appointed in Oct, 1950 to consider and report on amendments necessary to the Indian Companies Act, 1913, as amended by Act XXII of 1936, having due regard to the conditions necessary for the healthy growth of joint stock companies and the desirability of adequately safeguarding the interests of investors and the public.

The Report is the first comprehensive review of the Indian Companies Act undertaken since 1913. From the point of view of the committee, the major problems of company law reform in this country are those relating to —

- (i) the manner in which companies are promoted and formed—with particular reference to the law about prospectuses, minimum subscription and allotment of shares
- (ii) the nature and scope of the control exercised by shareholders on the management of a company ;
- (iii) the powers and functions of directors and the control exercised by them over the companies and their managing agents ;
- (iv) the terms of appointment and conditions of service of managing agents and their powers and functions *vis-à-vis* the directors of a company and the general body of shareholders
- (v) the powers of investigation and inspection conferred on the Government in cases of gross mis-management of the affairs of a company.
- (vi) the manner in which company accounts are kept and audited ,
- (vii) the position of minority shareholders and the protection to be accorded to them ;
- (viii) the rights of shareholders and creditors in winding-up companies ; and
- (ix) the administration of the Indian Companies Act, including the need for an authoritative body to keep a close and continuous watch on investment markets.

Basic ideas* :

The Committee's recommendations which cover the entire field of company law appear to be based on the following basic principles which the Committee stresses more than once in its report :—

(i) that the provisions of the law both in regard to the formation and management of joint stock companies should be as would ensure the maintenance of a minimum standard of behaviour in company promotion and management, but do not impose needlessly irksome or rigid rules which may hamper legitimate business or affect initiative or enterprise ;

(ii) that the law should provide for the fullest possible disclosure in prospectuses or statements in lieu of them before a company is formed and that failure to make such disclosure should be visited with effective penalties ;

(iii) that company accounts should be prepared in such a way that they disclose all facts which are material to a full understanding of the manner in which companies are worked ;

(iv) that company meetings should be called and conducted in such a way that shareholders receive all reasonable facilities for exercising intelligent judgement on the activities of the management ;

(v) that the provisions for investigation into the affairs of a company should be so designed as to enable an appropriate authority to intervene in its affairs not merely when an offence has been committed, but also when it is established that the affairs of company are being managed in a manner prejudicial to the shareholders of the company or to any substantial portion of them or when such investigation is otherwise necessary in the public interest ;

(vi) that the law should also provide for the establishment of an appropriate authority not merely for enforcing the provisions of the Companies Act or for carrying out the investigations which may be necessary under it, but also for generally overseeing the administration of the Act and for exercising that reserve of authority in the public interest, which must necessarily vest in some organ of Government.

Company promotion and formation :

Following the above general principles, the Committee recommends that the particulars which have now to be disclosed in

* Commerce, dated 15th. March, 1952.

a prospectus should be enlarged to include several matters on which at present very little information is given. It should disclose, for example, the previous consent of experts to citation of their opinions or views in a prospectus issued to the public. It should enclose copies of all material contracts entered into by promoters, vendors or others during the two years prior to the issue of the prospectus; and thirdly, the subscribed capital of the managing agency company, where a company is proposed to be managed by a managing agency company should be disclosed in the prospectus.

The Committee recommends the tightening up of the conditions laid down in section 92 of the present Act for the registration of a prospectus and also the provisions relating to minimum subscription in section 101 of the Act. In the Committee's views, the ease with which mushroom companies have been floated points to the need for imposing some obligations on directors for instituting thorough enquiries into the capital investments of the concerns. The amendments which the Committee proposes to the present law relating to minimum subscription are intended to prevent such floatations.

An important recommendation of the Committee under this head is that when a company states in its prospectus that an application has been made or will be made to a stock exchange for quotation of the shares or debentures offered for subscription, it should be required to apply to a recognised stock exchange for permission to deal in shares and debentures within ten days of the first issue of the prospectus. If no such application is made or permission to deal is refused by the authorities of the stock exchange concerned before the expiration of three weeks from the day of the closing of the subscription lists, the moneys received from the subscribers should be refunded to them forthwith.

The Committee also recommends that the Controller of Capital Issues should refuse to accord sanction to the issue of new capital, unless the prospectus conforms to the statutory requirements as to its contents. It is necessary, in the Committee's view, that some responsible authority should scrutinise the statutory information required to be disclosed in a prospectus before it is registered and issued.

Capital structure of companies :

Two important recommendations of the Committee relating to the capital structure of companies, in future, deserve particular

mention. The Committee recommends that, in future, the capital of a company should consist of only two broad categories, viz, equity capital and preference capital and the voting rights in respect of share capital should be strictly in proportion to the capital paid or credited as paid thereon. In the case of preference shares, such voting rights should, however, be exercisable only under certain contingencies. No other class of shares which confer any rights as to dividend, capital, or voting power disproportionate to the rights attaching to the ordinary shares should be issued. As regards existing companies which have issued shares with such disproportionate rights, the Committee recommends that they should, so far as the voting rights of such shares are concerned, bring them into proportion with the capital paid up on them within a period of three years from the passing of the new Act.

The other recommendation of the Committee is in regard to allotment of further issues of capital by a company. It recommends that the present section 105C of the Act should be suitably amended to provide that the additional issues of the capital by a company should be offered to the holders of equity capital in proportion to their holdings of such capital with a right to renounce the whole or part of this offer in favour of a third party. This provision will ensure that additional issues of capital by a company are made in such a way not to jeopardise the interest of the shareholders in the undertaking.

Company meetings and proceedings :

The Committee attaches maximum importance to the enactment of suitable provisions for the holding and conduct of company meetings, so as to enable active and competent shareholders to take effective part in the business transacted at such meetings. The Committee considers the provision of such facilities to be one of the sure safeguards against arbitrary action by the management. The general effect of its recommendations on this subject is to set out more precisely than is provided in the present Act, the place, time and the manner in which general meetings should be called and conducted in future. In particular, the Committee suggests detailed provisions regarding the period of notice, the service of notice, the demand for poll, the use of proxies and the preparation of the minutes of these meetings in such a way that they record faithfully all important business transacted in them.

One major change suggested by the Committee under this head is the abolition of extraordinary resolutions. As the Committee recommends a uniform notice period of 21 days, in future, for all resolutions to be moved in general meetings, it does not consider that any useful purpose would be served by providing for "extraordinary resolutions" and recommends their replacement by "special resolutions" as defined in the Indian Companies Act.

Directors :

The Committee's recommendations on directors constitute, in its own language, the "key to the reform of company law." Under the Indian Company law as in the English law, directors occupy a pivotal position in the structure of joint stock companies. They are not only the agents but in some sense also the trustees of the company. It is on these two fundamental concepts relating to the position of directors that the Committee has based its recommendations. Briefly, these are designed to ensure .—

(i) the constitution of independent boards representing the interests of the managements as well as of shareholders but without the dominance of the former over the latter ;

(ii) the selection as directors, of active individuals who can devote sufficient time and thought to the work of companies which they are supposed to direct ;

(iii) the adequate exercise of control by directors over the managing agents, where the day-to-day management of companies is in the hands of the latter ; and

(iv) the prevention of the misuse by directors of powers which they are entitled to exercise under the law but which past experience shows require careful control, e.g., the power to make loans to other directors, the power to enter into contracts, the power to sell, lease or otherwise dispose of property, the power to remit or extend the date of repayment of debt, and the power to borrow.

Minimum number prescribed :

As regards the constitution of a board of directors, the Committee disapproves of the appointment of a body corporate as director, and prescribes a minimum number of directors for every company—three in case of a public and two in case of a private company. The amendment of section 83B, which the Committee suggests is designed to ensure that the board does not

become a packed body of men, who are merely nominees of or directly or indirectly under the influence of the managing agent of a company. The intention is not to debar such persons from offering themselves for election to the board under the two-thirds quota, but to require that they can be so elected only if—(i) a special notice, within the meaning of section 142 of the English Companies Act of a resolution suggesting the appointment of such persons as directors has been sent to the company and circulated by the latter to its members stating the nature of their association or connection with the managing agents, and (ii) at least 80 per cent of the votes of the members present in person or by proxy have been cast in favour of their election.

Emphasis on quality :

It is not, however, enough, in the Committee's opinion, merely to secure the independence of the board of directors ; it is also necessary to ensure that only such persons are appointed who can devote sufficient time and thoughts to its work and are physically and mentally active to take an intelligent interest in a company's affairs. The Committee points out that in course of its examination of witnesses several instances were cited where directors by reason of their age were unable to take any active interest in the management of the companies, and observes that in such cases not only does the retention of office by such directors serve no useful purpose but also stands in the way of more active persons being elected to the board.

The Committee recognises that it is difficult to lay down any precise age limit but considers that, having regard to the circumstances in this country, it would be in the long-term interest of company management to fix an age limit for directors. It suggests that this limit should be 65. The Committee does not overlook the objection that in some cases persons above 65 may still retain their mental powers to such an extent as to justify their seats on a board, but as the Committee observe elsewhere, legislation must be always based on average behaviour. In any case, the Committee points out, this recommendation will not prevent the utilisation of the services of average directors in a different capacity, e.g., as adviser or consultant.

The other recommendation of the Committee which seeks to achieve the same object is that the number of directorships which a

person can hold should not exceed 20. After a detailed review of company practice in several countries, the Committee comes to the conclusion that in very few countries do persons hold more than a limited number of directorships. In the circumstances of India, however, it considers it necessary to fix the number fairly high, and suggests that it should not be reduced below 20.

Disqualifications of a director :

The recommendations of the Committee relating to the disqualifications of directors and the disclosure of directors' interests are similarly designed to improve the quality of directors and to secure their integrity. The committee recommends that an interested director not take any part in the proceedings of a board meeting in which contracts or arrangements in which he is concerned are being discussed and that all directors should be required to disclose the number, description and amount of shares in and the debentures of a company or of any other body corporate, being the company's subsidiary or the holding company or a subsidiary of the holding company, which are held by or in trust for them or of which they have a right to become holders whether by payment or not.

Relationship between directors and managing agents :

In the scheme of relationship between directors and managing agents which the Committee visualises, the superior position of the former is sought to be assured by the requirement that the most important financial and administrative powers which are necessary for the management of joint stock companies should be reserved for directors and exercised by managing agents only if they are delegated to them by the directors, except that a few specified powers should not be delegated in any event. These are :

- (i) the power to issue debentures ;
- (ii) the power to make calls on shareholders in respect of moneys unpaid on shares of the company ;
- (iii) the power to borrow moneys except within limits previously fixed by the directors at a board meeting ;
- (iv) the power to invest the funds of the company ; and
- (v) the power to make loans except within limits previously fixed by the directors at board meeting.

The recognition of the paramount position of directors in the management of a company does not, however, prevent the

Committee from recommending that some of the powers of a company, to which reference has been made above, should be exercised only by the company in general meeting and that some definite limits should be imposed on their other powers and activities relating to the grant of loans to directors, the holding of office or place of profit in a company or in its subsidiary and the sale, purchase or supply of goods by the directors to a company. The Committee's recommendations on the subject attempt to tighten up the provisions of the existing law which, as it observes, have been more honoured in the breach than in their observance. The Committee expresses the hope that its recommendations will not only prevent many current abuses and malpractices but also strengthen the position of directors *vis-à-vis* the managing agents and rehabilitate the position of the former as the ultimate depository of power and influence in a company.

Managing agents :

To the controversial subject of managing agents the Committee devotes one of the longest chapters in its Report. After a rapid survey of the development of the managing agency system in this country and a close analysis of the factors which have contributed to its growth, the committee concludes that notwithstanding the many abuses and malpractices which have disfigured the working of this system, in the present state of the industrial organisation of the country it may still be on balance, an advantage to continue to rely on it. For, as the Committee puts it, shorn of these abuses and malpractices the system may yet prove to be a potent instrument for tapping the springs of private enterprise.

The Committee, however, fully recognises that the adequacy and effectiveness of the system will, in future, depend not merely on the promptitude and thoroughness with which the evils which have clung to it are removed, but also on the energy, enthusiasm and foresight with which the managing agents conduct their business. That is, however, a matter essentially for managing agents and the recommendations of the Committee are concerned primarily with the lightening up of the provisions relating to managing agents in the present Indian Companies Act, so that opportunities for current abuses and malpractices may be reduced to a minimum. The main directions in which the Committee considers amendments to the present Act necessary are in regard to the appointment of managing agents, the conditions of service of managing agents,

the remuneration of managing agents, the powers of managing agents *vis-a-vis* directors and the activities of managing agents in regard to borrowings, loans, contracts, sales and purchases made on behalf of the managed company.

Appointment of managing agents :—

As regards the appointment of managing agents, the Committee recommends that in future managing agency agreements should be limited to 15 years, subject to renewal for a period of 10 years and that no reappointment of the same managing agent should be made except during the last 24 months of the outgoing period, in regard to existing managing agency agreements, unless they run out earlier, the Committee recommends that they should all expire on the 15th August, 1959. The Committee has fixed this date as it will leave a reasonable period of time after the new Act comes into force for the existing managing agency agreements to expire.

As regards the removal of managing agents, the Committee recommends that an ordinary resolution of the company should suffice in the case of fraud or breach of trust, while in other cases a special resolution would be required, but no resolution should be required to dismiss a managing agent who has been convicted of a non-bailable offence. Certain safeguards are, however, provided for managing agents which are firms or companies.

As regards the transfer of managing agents, the Committee recommends several restrictions on such transfers which are intended to remove current evils of trafficking in or cornering of managing agency rights. The subject is not free from difficulty, and the Committee frankly admits this when it says : "We experienced considerable difficulty in reconciling what we consider to be the fundamental right of a managed company to be managed by the managing agent whom it has appointed and not by some third party who in fact might have acquired a controlling interest in such managing agency firm or company with the undesirably of imposing such rigid conditions on the acquisition of an interest in a managing agency firm or company as might preclude the introduction of persons into such firms or the acquisition of interest in such companies by persons who might be able to contribute towards the management of the managed company." But the Committee expresses the hope that its recommendations coupled

with the provisions which it has suggested in the Report, regarding the enforcement of the rights of minorities, the disclosure by directors and persons deemed to be directors of their holdings in a company and the power of investigations into the ownership of shares, will provide a salutary check on any large-scale traffick in managing agency rights in future

Remuneration :

On the subject of managing agency remuneration the Committee recommends that the commission which managing agents would be entitled to draw in future should not in any case exceed $12\frac{1}{2}$ per cent on net profits, and the expression "net profits" will have to be very carefully defined. This the Committee has attempted in its elaborate redraft of the present section of the Act dealing with this matter. The Committee has also recommended that no office allowance would be admissible to managing agents, but they would be entitled to be reimbursed by the company for any actual expenditure incurred on the maintenance of their office. Further, the Committee has suggested that in the event of absence or inadequacy of profits, the managing agents would be entitled to such minimum remuneration as is considered reasonable by the company in a general meeting subject to a maximum of Rs. 50,000 per annum, but no other additional payment in any other form would be admissible to them. The Committee further recommends that the remuneration of all existing managing agents should be brought in line with its recommendations within a period of two years from the enactment of the new Act.

As regards compensation for loss of office the Committee recommends that no compensation will be payable to managing agents if they resign or if the managing agency is terminated for reasons which would justify their removal or if they are parties to a resolution procuring such termination. In other cases compensation would be limited to the average earnings for a period of five years or such lesser period for which they may have held their office.

The Committee pleads for a complete reorientation of ideas as to the position and powers of managing agents. In its view, managing agents should act only under the general control and direction of directors, but subject to this control, their powers and duties should be clearly laid down so that within their sphere

they are free to carry on their duties. The specific approval of directors would, however, be required to certain acts enumerated in a schedule, e. g., the power to appoint managers, the power to engage staff except within the limits fixed by directors, etc. As has been already noted, the Committee also disapproves of the delegation of certain specific functions to managing agents, e. g. the power to issue debentures, the power to make calls, the power to borrow money or to invest the funds of the company or to make loans, except within limits fixed by directors.

With regard to some of the existing powers of managing agents, e. g., the powers to make loans, to enter into contracts, etc., the Committee suggests extensive amendments to the present provisions of the Act similar to these proposed in the case of directors. As regards the managing agents' power of investment in another company, under the same management, the Committee recommends that the limit on such investment should be 10 per cent. of the subscribed capital of all the investment companies in the group as a whole.

The Committee also recommends that the managing agents should not in future be entitled to any commission on purchases made on behalf of the company, but they should be entitled to charge a small commission as may be approved by the company by special resolution, for the distribution of the products of the company provided they were appointed as distributors in a general meeting and had already held a place of business in areas for which they were so appointed. The Committee has also tightened up the provisions of the present Act relating to the powers of managing agents to engage in business which is similar to and directly competes with the business of the managed company. In the Committee's opinion, the present provision has been much abused in the past, and in the interest of the managed company it is essential that the present law on the subject should be tightened up.

Accounts :

In the provisions of the present Act relating to accounts, the Committee suggests extensive amendments some of which embody the provisions of the English Act of 1948, while others go beyond it. In regard to these amendments, the Committee points out that the provisions of the Indian Companies Act relating to accounts and audit have been always in advance of the corresponding

provisions of the English Act and observes that the amendments which it has suggested have been inspired not merely by theoretical preference for advanced legislation but as a matter of practical importance. For, it is only by the fullest measure of disclosure in company accounts that the financial position of a company and its state of affairs as a going concern can be correctly assessed.

The Committee dismissed the usual objection against making fuller disclosure of particulars in company accounts by the tart observation that as long as company accounts do not reveal the unit cost of production of a commodity, there can be no legitimate objection on the part of the management to disclose the fullest information in the balance-sheet and the profit and loss account. The detailed recommendations of the Committee regarding the contents of these documents, will, it is hoped, enable, in future, discriminating shareholders to exercise adequate control over the affairs of a company. Provided these provisions are effectively enforced, there is little risk of shareholders' control being rendered illusory by the dearth of essential information in company accounts about the management of companies.

The other recommendations which the Committee makes about company accounts relate to :—

(i) the facilities for the inspection of books of account by directors ;

(ii) the adjustment of the accounting period so as to bring it into line with the Committee's proposals under section 76 of the Indian Companies Act regarding the period during which the annual general meeting of a company must be held ;

(iii) the manner in which and the period for which the statements of accounts of a subsidiary company will have to be prepared. It has been suggested in the redraft of section 132A that this statement must not relate to a period earlier than six months from the date of the financial year of the holding company; and where the dates of the financial year of the holding company and the subsidiary company are not the same, the further disclosure of the financial position of the subsidiary company for the intervening period which is not covered by the above provision has to be provided ;

(iv) the vesting of authority in the Central Authority for a change in the accounting period of a company in order to obviate hardship or difficulty in special cases ;

(v) the requirement that directors must approve of the accounts before they are placed before the auditors and that an auditor's report should be annexed to the accounts ; and

(vi) the requirement that, in modification of section 134 of the Indian Companies Act, all documents annexed to the statement of accounts besides the balance-sheet and the profit and loss account would have to be filed with the Registrar.

Audit :

The amendments which the Committee suggests in the provisions of the Act relating to audit and auditors are primarily designed to secure the independence and integrity of the latter. As the Committee observes, the two basic qualifications of auditors needed for the purpose of company law are that they should be professionally competent and that in the performance of their duties they should show integrity and independence of judgement. No law, however, which the Committee observes, can ensure these qualities but the object of the amendments is to create conditions under which auditors, provided they are technically competent and possess natural integrity, should be able to discharge their statutory duties without fear or favour.

One of the important recommendations of the Committee is thus that certain categories of persons who are closely connected or associated with managing agents should be debarred from appointment as auditors. The power of management to appoint, reappoint or remove auditors are also greatly circumscribed and the shareholders are given a very much larger say in these matters than they have at present, while the auditors are given the right of access to the shareholders in general meetings and the right to represent their cases when occasion demands.

Inspection and investigation :

No other aspect of the present company law has received so much adverse comment as the present provisions relating to the inspection and investigation of the affairs of a company. The two criticisms which were generally made by witnesses appearing before the Company Law Committee were the inadequacy of the provisions of the present Act and their inadequate administration. The

Committee admits these charges, but observes that the defective working of the present Act is not merely due to the ineffectiveness of the existing administrative machinery, but also to a large extent to the lacuna and loopholes in the existing provisions as embodied in section 137 to 143 of the Act. It suggests a thorough overhaul of these provisions on the lines of sections 164 to 171 of the English Act, 1918.

The most important changes resulting from the recommendations of the Committee on this subject are that the appropriate authority would be able to initiate investigation into the affairs of a company not only on the application of a specified number of shareholders but also on its own motion, where the company by a special resolution or the court by its order, or the appropriate authority as a result of information received by it or informal enquiries conducted by it considers that such investigations should be held.

The powers of the investigators are also considerably enlarged. Inspectors are empowered to call for documents, examine officers and agents of the company on oath, provided the court orders such examination. The appropriate authority can also take criminal action on behalf of the company for recovery of damages in respect of any fraud, misfeasance or other misconduct in connection with the company. The inspector's report, if duly authenticated, would also be admissible as evidence in any legal proceedings.

Any new provision recommended by the Committee is the insertion of a provision enabling an appropriate authority to investigate into the ownership of shares in or the debentures of a company. Sections 172 to 175 of the English Companies Act confer such powers in suitable cases on the Board of Trade, and the Committee recommends that the proposed Central Authority for the administration of the Indian Companies Act should also assume similar powers. If the Committee's recommendations are accepted, they will enable the Central Authority to determine the facts relating to changes in the controlling interest of a company, where such determination is necessary.

New principles :

Two further recommendations of the Committee under this head introduce new principles into the Indian Companies Act.

The Committee suggests that having regard to the special nature of offences under the Indian Companies Act, the Companies Act should provide, in modification of the principles underlying the Criminal Procedure Code, that a person accused of any offence under the Companies Act may become a competent witness, relating to such offences. The Committee observes that in many cases successful prosecution of offences under the Indian Companies Act is now hindered by the fact that material information relating to certain matters, which are within the knowledge of or in the possession of an accused person is not available to the court, because under the existing law the accused is not a competent witness. In its view, the considerations on the basis of which under the existing criminal law the accused person is debarred from appearing as a witness do not apply to offences under the companies Act. Under the Committee's recommendation, an accused will not be compelled to appear as a witness, but if he fails to do so it will be competent for the court to take this fact as a circumstance which along with the other circumstances of the case the court is entitled to take into account in arriving at its finding, and further, if in such cases the accused person does appear before the court as a witness, he will be liable for any false statement that he may make as any other witness appearing before the court. The Committee feels that this provision would be a salutary check on unscrupulous persons.

The other important recommendation is an adaptation of the well-known sec. 210 of the English Companies Act, 1248, which provides for an alternative remedy in lieu of winding-up in the case of oppression to a minority of shareholders. Under this section of the English Act, the Court has power, without winding-up the company, to impose on the parties to a dispute, in a case of oppression of minority shareholders, whatever settlement the court considers just and equitable. What constitutes oppression would be a matter of fact to be determined and the court's finding on this point is conclusive. The reason why this alternative remedy was provided for in the English Companies Act, 1948, was that in many cases the ordinary remedy of winding-up the company would not benefit the minority shareholders, since the break-up value of the assets might be small or the only available purchaser might be that very majority whose oppression had driven the minority to seek redress. The provisions of this section have been

incorporated, with necessary adaptations to suit Indian conditions, in the Indian Companies Act, 1951 (*vide* sections 153C and 153D).

Other recommendations :

The other recommendations of the Committee cover a wide range of subjects to which only a passing reference can be made. The Committee suggests considerable strengthening of the present provisions of the Act relating to preferential payments, fraudulent preference and offences committed before or in course of winding-up proceedings and several important changes in the present procedure relating to liquidation proceedings. It also recommends that.

(i) permanent official liquidators should be attached to all High Courts and that winding-up cases in respect of companies with a subscribed share capital of Rs. 1 lakh or more should be instituted only in the High Courts ;

(ii) that suits in respect of arrears of call should be decided by summary proceedings, and

(iii) that all suits by and against that company in winding-up should be instituted in the court in which the winding-up proceedings are pending.

Another recommendation of the Committee is in respect of the regulations governing a company. It recommends that several existing regulations should be made compulsory and that some new compulsory regulations should be incorporated in the Act. All compulsory regulations should in its view form regular sections of the Act and should not be liable to be altered by Government except by an amendment of the Companies Act.

Administrative Machinery :

The problems relating to the administration of the Indian Companies Act cover the last part of the Committee's Report. After describing at considerable length the present system of administration, the Committee proceeds to elucidate its recommendations as to the reorganisation of the existing machinery for the administration of the Indian Companies Act. Chapter XVIII of the Committee's Report deals comprehensively with the subject.

Main directions of reform :

Following a searching analysis of the defects and deficiencies of the existing system, the Committee comes to the conclusion that

the main directions in which reform of the present administrative machinery are necessary are as follows :—

(i) The administration of the Indian Companies Act together with the establishment of the Registrars should be brought under Central Control and direction.

(ii) This control should not, however, be exercised departmentally but by a duly constituted authority set up under the Companies Act.

(iii) The office of the Registrar of Joint Stock Companies should be strengthened by the appointment of whole-time Registrars in all areas. For this purpose it may be necessary to group a number of States under one charge. Indeed, the Committee visualises the division of this country into a number of suitable regional units each in charge of a whole-time Registrar, assisted by Additional or Assistant Registrars, as the case may be, wherever necessary.

(iv) The Registrars should carry out the functions statutorily imposed on them under the Act, but under the general control and supervision of the proposed Central Authority. They will also act as agents of this Authority for such other functions relating to the formation and working of joint stock companies or related subjects as may be entrusted to them.

(v) In order that the Registrars can discharge their duties effectively, it will be necessary to raise the status of their office so as to attract the right type of men to fill them up.

Central Authority :

The Central Authority, which the Committee designates as the Corporate Investment and Administration Commission, forms the pivot of the Committee's scheme for the reorganisation of the administrative machinery. Explaining the necessity for such a Central Organisation, the Committee observes that the main reason for the under-administration of the present Companies Act is the absence of any well-knit and competent organisation at the Central for administering a difficult and complicated piece of legislation like the Companies Act and no reforms in company law, however, well designed, will be of any avail unless a strong and competent administrative machinery to over-see its working and enforce its provisions has been established. The Registrars in the different

States have been no more than filing officers, concerned only with the formal registration of documents presented to them.

The absence of any competent authority either at the Centre or in the States to supervise the administration of the Act has resulted in widespread abuse or perversion of its provisions, and at the same time prevented any systematic examination or study of current trends in company practice. This has been a source of considerable weakness in the economic administration of the country, and the only way in which, in the Committee's opinion, this serious lacuna in the administrative system can be made good is by the appointment of a competent and high powered organisation at the Centre.

Composition .

The Committee recommends that this body should consist of a chairman and four members whose qualifications and standing should be such as to inspire general confidence. They should be men of appropriate status and standing who should be able to combine among them suitable administrative experience, practical knowledge of company law and of company accounts and finance, and should be selected primarily on the basis of their competence for the functions which they will have to perform together with their standing in the service, profession or other occupation in which they may be engaged.

Functions :

As regards the functions of the Commission, the Committee recommends that it should carry out all such duties relating to the administration of the Companies Act, including in particular—

(i) the exercise of the powers of inspection and investigation which the Committee has recommended in Chapter XII of its report;

(ii) the exercise of the powers and duties arising from the accounts provisions of the Act ;

(iii) the supervision of winding-up proceedings, where this authority is conferred on it ;

(iv) the study of balance-sheets and profits and loss accounts of companies with a view to determining to what extent they conform to the requirements of the Act.

The Commission should also keep the investment market in the private sector under continuous observation. For this purpose it would have to undertake a systematic study of prospectuses, of the terms and conditions of new issues of capital, of company accounts and of qualified reports by auditors of companies, and should bring to the notice of Government any new trends in company management that might require their attention.

The Committee further recommends that the Commission should be entrusted with the functions relating to capital issue control which are now performed by the Controller of Capital Issues and those connected with the regulation of stock exchanges and indeed with all matters relating to the promotion, formation and working of joint stock companies. In the Committee's view, the case for the co-ordination of capital issue work with that relating to company formation and company management is overwhelming, while the delegation of work relating to the regulation of stock exchanges would prevent multiplicity of authorities and ensure the maintenance of much-needed link between the management of companies and the working of stock exchanges. In this connection the Committee points out that the functions relating to the stock exchanges both in the U. K. and the U.S.A. are dealt with by the same organisation as is responsible for the administration of the Companies Act and the supervision of joint stock companies, viz, the Board of Trade in the U. K. and the Federal Securities and Exchange Commission in the U. S. A.

An interesting suggestion of the Committee is that the proposed Central Authority should be charged with the duty of building up a cadre of trained technical administrative staff competent to analyse and study prospectuses, company accounts and problems of investment finance, and that one of its first tasks as soon as it is constituted should be to reorganise company statistics on more systematic and rational lines and to present them in a form, which would lend itself to meaningful analysis of economic trends in private sector of the country's economy.

In its concluding chapter, the Committee makes a strong plea for a comprehensive consolidating Companies Bill. It observes that a comprehensive measure is long overdue and should be taken in hand as early as possible.

The Committee concludes with the hope that, when the changes which it suggests in the Companies Act have been fully introduced, and the Central administrative machinery which it recommends has been set up and adequately equipped for its difficult task, the reforms which it has recommended both in law and administration will go far to improve company practice in this country. The Committee recognises that some of the restrictions on company management which it has recommended may appear irksome to business which is conducted in efficient and honest manner, but feels confident that none of them will impose any unreasonable burden on legitimate business. In any case, the inconveniences and hardship that may be caused to some concerns by the enforcement of its recommendations will, in the Committee's view, be more than compensated by the general rise in the average standard of business management in this country.

Test And Examination Questions

(On Problems of Management)

1. "The principal object underlying the appointment of directors is to ensure proper control and supervision over the management by the Managing Agents. But such control and supervision have proved ineffective because shareholders do not possess real voice in the appointment of Directors). ("Memorandum of Bombay Shareholders' Association on Directors"). Discuss the views contained in the above statement.

2. How are the directors of joint stock companies selected and appointed in India ? (Agra, B Com. 1946).

3. What are the influences which help to increase the concentration of powers in the hands of the directors of a joint stock company ? (Bombay, B. Com. 1935).

4. The Managing Agency System has outlived its utility in India ? Do you share this view ? (Cal. M. Com. 1945).

5. In what ways may the shareholders of a limited company exercise control over its affairs, and to what extent is their control real in this country ? (Agra, B. Com. 1945).

6. In a joint stock company what control is exercised and what responsibilities are borne by (a) shareholders, (b) directors and (c) managing agents ? (Bombay, B. Com. 1934).

7. What are the rights of the shareholders of a joint stock company ? How far do those rights enable the shareholders of a joint stock company ? (Bombay, B. Com. 1941).

8. Attempt an essay on the "Problems of joint stock company management."

9. Briefly summarise the Company Law Committee Report.

10. Write full notes on any one of the following :—

- (a) Profit Sharing Scheme.
 - (b) Management of Production.
 - (c) Management of Labour.
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BOOK THREE

Company Secretarial Work



CONTAINING

Position, powers and duties of Secretary;

Company Secretarial Practice;

All about different kinds of

meetings, procedure thereat

and conduct thereof

kinds of resolution;

Reconstruction

amalgamation

E t c. E t c.



"The Secretary

is a mere servant;

his position is that he is

to do what he is told, and

no person can assume that he has

any authority to represent anything

at all."

—'LORD ESHER'

CHAPTER I.

SECRETARY AND HIS DUTIES

Who is a Company Secretary ?

The Secretary of a company is to all intents and purposes its agent, who is responsible for the secretarial work; but it is not necessary that he should always be called secretary. In India, a large number of companies are managed by managing agents, who also look after the secretarial work of the companies under their control. Similarly, in many banks and insurance companies, the secretarial work is done by the director, manager or managing director. So the name is immaterial, function is everything. Anybody responsible for the secretarial work is the secretary of that company, by whatever name called. A Secretary is included within the definition of the term "Officer" as given in sec. 2 (I) (II) of the Act.

The term 'Secretary' is, indeed, derived from the Latin word 'Secretarius', which stands for a notary or scribe. In early days it was employed in connection with secretaries privately employed by Ministers of State. Thereafter, it has extended to Secretaries of Embassies and Legations and even private individuals with large estates. With the advent of joint stock companies, however, he began to be employed by such concerns also.

Position of a Secretary :

The position of a company secretary is not defined by law: but it can be inferred from the various provisions of the Indian Companies Act as also the Indian Income Tax Act. Usually he is entrusted with the work of taking down the minutes, circulating the agenda and doing other works in connection with Board, Meetings. He is in many respects the 'Brains' and 'Hands' of the company. His position has been correctly summed up by Lord Esher in the following words :—

"The secretary is a mere servant; his position is that he is to do what he is told, and no person can assume that he has any authority to represent anything at all."

In this respect he must obey the orders of the directors and must not do that which he knows to be wrong to, or a fraud upon another person.

Duties of Secretary :

The duties of a company secretary vary according to the nature and size of the company he serves. He is the most important executive officer of the company and is, in fact, the mouthpiece and instrument of the company so far as any ministerial acts are concerned. As a confidential servant of the company he is entrusted with the common seal of the company, and the confidence of the directors.

As a 'routine' officer, his duties may be enumerated as follows :—

(1) He must see that all the books required to be kept under the Act, are properly maintained and written.

(2) He must act as 'clerk' to the Board, recording its minutes and decisions and also those of the company; and for this purpose he should take down notes of what transpires at such meetings.

(3) He should prepare and issue notices and agenda of meetings.

(4) He should receive notices on behalf of the company. But, if the same person is the secretary to two companies, knowledge acquired by him as secretary of one company cannot be treated as the knowledge acquired by secretary of the other company, unless there is duty to indicate the knowledge. Similarly, a notice received by the secretary, when not received in the course of company's business or under such circumstances that it is his duty to communicate to the company, is not a notice to the company.

(5) He must make all necessary returns to the Registrar of the companies.

(6) He is also responsible for the correspondence of the company.

(7) He should supervise all issues of capital and debentures.

(8) He should keep ready for delivery the share certificates within the prescribed time.

(9) He should prepare, issue and pay dividends.

(10) He should certify valid transfers.

Rights and powers of a Secretary :

As head of the secretarial department, a company secretary is entitled to superintend, direct and control it. He is the clerk or servant of the company entitled to rank as preferential creditor under sec. 230 of the Act, if he gives his whole time to the company, but not when he performs his duties by a deputy. Section 150 further empowers him to sign a document or proceeding requiring authentication by the company.

A secretary has no power to bind the company by a representation as to the affairs of the company so as to induce people to purchase shares. Accordingly, a person induced by a fraudulent misrepresentation of the company secretary, cannot maintain an action for rescission of contract or for damages against the company.

The secretary also does not possess the power to register a transfer until it is passed by the directors of the company or to convene a general meeting unless authorised by the Board of Directors to do so; nor to strike off a name from the register of members. Again, he has no right to take any improper commissions, and if he does so, misfeasance proceedings may be started against him. Where a chief officer, such as the managing agent, appoints a secretary with powers of management of the company, such a secretary can, if so empowered by the chief officer, institute a suit on behalf of the company. A secretary cannot, however, be allowed to treat a resolution dismissing him from his post passed by the company in general meeting, as void, even if the same is irregular for want of proper notice.

Liabilities of Secretary :

If the secretary makes default in complying with the requirements of the Indian Companies Act, he shall be liable for numerous penalties. As an officer of the company, he is liable for his wilful misconduct or negligence. A secretary, who also acts as a Manager, is liable for negligence in preparing false balance-sheets and accounts causing dividend to be paid out of capital. He is also liable for misfeasance, if he receives an improper commission, but unlike directors, he shall not be personally liable for the misapplication of the company's fund.

Qualifications of a Secretary :

In order to be able to carry out his onerous duties successfully, it is essential that a company secretary should be a 'big' man. He

must possess a sound knowledge of Company Law, secretarial work, Accountancy, Taxation and other mercantile and industrial laws affecting the business of the Company. Besides this, he should also possess a thorough knowledge of the Memorandum and Articles of the Company and be fully conversant with the duties imposed on directors in order to be able to assist them on technical matters. A Company secretary should have a sound general education, a working knowledge of trade, command over English language and above all fine traits of character. He should be a man of good judgement, tact and experience. His advice may be sought from time to time in regard to the investments of the company, and might also be consulted on questions of policy and administration. The first part of the word Secretary means that he is the "Keeper of Secrets". He is a confidential servant of the company, and must, therefore, be discreet in his talk so that any important information may not leak out accidentally or involuntarily.

The duties of the company secretary will now be considered in detail in the following chapters.

CHAPTER II.

ISSUE OF CAPITAL, CALLS Etc.

Pri-Inccorporation duties of Secretary :

Prior to the incorporation of a company all the preliminaries are performed by promoters, and the secretary who is engaged as a protem officer may be asked to assist the promoters in the preliminary work. It should, however, be noted here that this work he does in an unofficial capacity and it is only after incorporation that he comes on the scene officially. He may be asked to attend all preliminary meetings convened by the promoters, to keep a record of the proceedings of these meetings and assist in the drafting of the various statutory documents required to be filed at the time of incorporation. The legal formalities to be complied with at the time of incorporation have already been described in detail in Book One.

Preliminary duties post to incorporation :

After the incorporation of a company, the first duty of the secretary is to organise his office systematically. The ideal to be kept is the maximum of efficiency with the minimum of waste. Further, he should distribute the work with such tactful diplomacy as to maintain feelings of esprit de corps amongst his personnel. He should be a good psychologist also—able to read the character of each and every member of his staff. This quality will help him a lot in organising his office-staff. He will be interested in them and will lend a sympathetic ear to their views and opinions. After arranging the office, the secretary should attend to the following duties :—

1. The name of the company must be kept painted or affixed in letters easily legible, and in a conspicuous position on the outside of every office or place where the company carries on business.

2. The name of the company must be engraved in legible characters on its common seal.

3. The name of the company must be mentioned in legible characters in all notices and other official publications.

4. He should arrange for a notice board to be set up in a conspicuous part of the office, and should see that all notices and

other information of interest to the members and the public are displayed there—on for such period as may be considered sufficient.

5. He should also keep a Seal Book, a specimen page of which is as below :—

No. of Minute authorising use of Seal	Date of Sealing	No. of documents sealed	Particulars of documents	Initials of Director or Secretary	Remarks

Secretary's work in connection with the conversion of a private company into public :

It has been stated in Book One that a company may be formed either as private or public. When a private company has been formed, and afterwards it is desired to convert it into a public company, the following procedure will be followed :—

1. The Company has to delete the clause in the Articles which restricts the transfer of shares; limits the membership to 50 and prohibits the offer of shares to the public. The alteration of the articles would be possible by passing a special resolution a copy of which must be filed with the Registrar of Joint Stock Companies within 15 days of the passing of the resolution. The Registrar thereupon, will make the necessary record in the register of companies maintained for the purpose.

2. The Company, then, will be required to file a Prospectus or a Statement in lieu thereof within 14 days of the alteration of the articles.

3. Then, the consent of the directors to act as such and their consent to take up the qualification shares and pay for them, must also be filed.

4. Finally a declaration under sec. 103 that all the requirements of the Act relating to public companies have been complied with, and the documents filed.

The following are the specimens of some of the documents required to be filed with the Registrar :—

1. List of persons who have consented to become directors :

The Indian Companies Act, 1913.

Filing Fee Rs. 3/-

Name of Company.....

List of persons who have consented to be Directors of the.....
to be filed with the registrar pursuant to section 84 (2).

Presented for filing by.....

To the Registrar of Joint Stock Companies.....

I/We, the undersigned, hereby give you notice, pursuant to sec. 84 (2) of the Act, that the following persons have consented to be directors of the.....

Name	Address	Description

Signature, address/and description of
applicant for registration.

Dated this.....day of.....195.....

2. Form of consent to act as directors :

The Indian Companies Act, 1913.

Filing Fee Rs. 3/-

Name of Company.....

Consent to act as Director/Directors of the.....
.....to be signed and filed pursuant to sec. 84 (1) (1).

Presented for filing by.....to the Registrar
of Joint Stock Companies.....

I/We, the undersigned, hereby testify my/our Consent to act as Director/Directors of the.....pursuant to sec. 84 (1) (1) of the Act.

Signature	Address	Description

Dated this.....day of.....195.....

3. Form of agreement to the qualification Shares :

The Indian Companies Act, 1913.

Filing Fee Rs. 3/-

Contract by directors to take and pay for qualification shares in..... Limited to be signed and filed pursuant to sec. 84 (1) (2) of the Act.

Presented for filing by.....

We, the undersigned, having consented to act as directors of the..... Limited, do each hereby agree to take from the said company and pay for the.....shares of.....each, being the number of shares prescribed as the qualification for the office of director of the said company.

Signature	Address	Description

Dated this.....day of.....195.....

Witness to the above signatures

Address

4. Form of statutory declaration :

ON REGISTRATION OF A COMPANY

(Sec. 24)

The Indian Companies Act, 1913.

Filing Fee Rs. 3/-

Name of Company..

Declaration of Compliance with the requirements of the Indian Companies Act, 1913, made pursuant to section 24 (2) on behalf of a company proposed to be registered as the.....

Presented for filing by I. of. do solemnly and sincerely declare that I am an Advocate / Attorney / a Pleader, entitled to appear before a High Court who is engaged in the formation of the company / a person named in the Articles as a Director / Manager / Secretary of the.....and that all the requirements of the Indian Companies Act, 1913 in respect of matter precedent to the registration of the said company and incidental thereto have been complied with, save only the payment of the fees and sums payable on registration. And I make this solemn declaration conscientiously believing the same to be true.

Note : The declaration need not be either.

(a) Signed before a Magistrate or an Officer competent to administer oaths, or

(b) Stamped as an affidavit.

5 Form of notice of situation of registered office :

Sec. 72

The Indian Companies Act, 1913.

Name of Company..

Presented for filing by

To the Registrar of Joint Stock Companies..

.. Limited,

hereby gives you notice in accordance with Section 72 of the I. C. A., 1913 that the registered office of the Company is situated

at.. / was removed

from.... to.. on

the.. 19..

Signature

Designation

Dated the.. day of.. 19..

(State whether Director, Manager or Secretary)

ISSUE OF CAPITAL

After the incorporation of the Company, the next requisite is the obtaining of capital, and this may be arranged either privately or by public subscription. A Company having an authorised capital of over Rs. 5/- lakhs cannot, according to D. I. Rule No. 94—A, issue its shares unless it has obtained the written consent of the Central Government. Where capital is to be raised by public subscription, the company issues a prospectus giving out the details as required in sec. 93 of the Act. Where prospectus is not issued, the company has to file a statement in lieu of prospectus. Very often application forms are attached to the prospectus, and the intending purchasers of shares are required to send them duly filled in with the application money to the company's bankers. The following is a specimen of the application form :—

.. .. . Limited

Issue of Shares

No.

To

The Directors,

.. .. . Co. Ltd.,

Gentlemen,

Having paid to the Company's bankers, the..... Bank Ltd. the sum of Rs. being a deposit of..... shares of Rs. each in the above named Company, I request you to allow me that number of shares, and I, hereby agree to accept the same or a smaller number that may be allotted to me upon the terms and conditions of your prospectus dated the.....to pay the balance as provided by the prospectus, and I authorise you to place my name on the Register of Members of the Company as the holder of the shares allotted to me. I hereby agree to accept such allotment of shares subject to the Memorandum and Articles of Association of the Company.

Name (in full)

Address (in full)

.. .. .

.. .. .

Profession or Designation

.. .. .

Signature

Dated

.. .. .

The allotment :

When the minimum subscription fixed in the prospectus according to law is obtained and the list is closed, the directors will proceed to allotment. A meeting of the Board of directors will be called and allotment will be made by recording a resolution which may be as follows :

“RESOLVED that the number of shares entered in the column headed ‘Shares Allotted’ of the Application and Allotment Sheets against the name and address of each applicant, be allotted to each applicant, making a total allotment of Rs. shares, and that a letter of allotment, stating particulars of the shares allotted and the amount payable on allotment, be sent to each allottee; and where no number of shares is entered in the ‘Shares Allotted’ column against the applicant’s name, that no allotment be made, and that the application money be returned to each applicant with a letter of regret.”

A minute of the Directors’ resolution should also be recorded in the Directors’ Minute Book. It should be noted that in case the minimum subscription has not been obtained, and allotment is not made within 180 days, the whole of the application money received must be returned within the next 10 days to the applicants.

Letter of allotment :

After allotment, the particulars thereof must be recorded in the Application and Allotment Sheets, and a letter of allotment, bearing a two-anna revenue stamp, be sent to each allottee. The following is a specimen of such a letter :—

Jiyajceerao Cotton Mills Co. Ltd,

Birlanagar,

Gwalior,

March 30, 1953,

Name and Address of
Allottee.

Dear Sir/Madam,

In response to your application dated.....you have been allotted.....shares of Rs. each in the Jiyajceerao Cotton Mills Co. Ltd.

The amount payable on application and allotment at
Rs. per share.

You have already paid.. . . .Rs.

Amount due from you on allotment Rs.

Payment of the amount due from you should be made on or
before.. . . .to.. . . .

Your faithfully,

.. . . .

Managing Agents

This form with remittance, must be forwarded entire to.. .
.. . . .who will return it duly receipted. It should then be
carefully preserved to be exchanged for the relative certificate in
due course.

No letter of allotment is necessary in the following cases :—

- WHERE : (i) The company offers a specified number of shares
to a person and he accepts them;
- (ii) Shares are issued by directors to themselves;
- (iii) A Company is reconstructed or amalgamated;
- (iv) An applicant waives notice of allotment;
- (v) An applicant has been made aware of the accep-
tance by the company of his application;
- (vi) A letter demanding payment has been despatched;

Letter of regret :

If the issue is oversubscribed and no allotment is made to some
of the applicants, a letter of regret should be sent along with the
cheque returning the application money. A specimen of such a
letter is as below :—

Jiyajeerao Cotton Mills Co. Ltd.

Birla Nagar,

Gwalior,

16th Sept., 1953.

.. . . .

.. . . .

.. . . .

Dear Sir/Madam,

I am directed to inform you that the Directors regret that
they are unable to allot you shares in the company in accordance with

your application dated... . Therefore, a cheque of Rs. . . . , being the refund of the amount paid by you, is enclosed herewith.

Please acknowledge receipt.

Yours faithfully,

Encls. (cheque).

for... . Co. Ltd.

Secretary.

Return of allotment :

With a month from the date of allotment, the company is required to file with the Registrar a return of allotment stating the following particulars :—

- (i) The names, addresses and description of the allottees;
- (ii) The amount, if any paid, or due and payable on each share;
- (iii) The number and nominal amount of shares allotted distinguishing the various classes of shares;
- (iv) Number and nominal amount of shares allotted for a consideration other than cash and the amount treated as paid on such shares;

In case of shares allotted as fully or partly paid up otherwise than in cash, a contract of sale is also required to be filed with the registrar. If default is made in complying with these requirements, every director, manager, secretary or other officer, who is knowingly a party to the default, shall be liable to a fine not exceeding Rs. 50/- a day during which the default continues.

After the completion of allotment, the secretary will arrange for the preparation of share register, and necessary entries will then be made in the Register of Members, in which a separate account of each member is to be kept.

Commencement of business :

Section 103 prescribes certain formalities, which are to be

already describe in Book I. It was mentioned there that a Statutory Declaration is also required to be filed with the registrar by the Secretary or one of the directors that the provisions of sec. 103 have been complied with. The following is a specimen of such a Declaration :—

FORM OF STATUTORY DECLARATION

Name Co. Ltd.

Declaration that the conditions of section 103 of the Act have been complied with.

Presented for filing by

I of being the Secretary/a director of the do solemnly and sincerely declare :—

(i) That the amount of the share capital of the company offered to the public for subscription is Rs.

(ii) That the amount stated in the Prospectus as the minimum subscription, which in the opinion of the directors, must be raised by the issue of share capital in order to provide for the matter specified in sub sec. 2 of sec. 101 of the Act is Rs.

(iii) That shares held subject to the payment of the whole amount thereof in cash have been allotted to the amount of Rs.

(iv) That every director of the company has paid to the company on each of the shares taken or contracted to be taken by him, and for which he is liable to pay in cash, a proportion equal to the proportion payable on application and allotment on the shares offered for public subscription.

I declare that the foregoing statements are true to my knowledge and belief.

Signature

Dated :

Secretary

CALLS

How call is made :

In making the calls, the procedure specified in Articles must be strictly followed otherwise the call may be declared to be invalid. Calls must be made by means of a resolution of a board of directors, and should be notified to the shareholders concerned. The

resolution must also state the time of payment and may be worded as below :—

“RESOLVED that a call of Rs. per share be made upon the partly paid shares nos. to such call to be payable on the date to the company's bankers Bank Ltd., and that the call notices be issued on the (date) to the registered shareholders.”

A call is deemed to have been made at the time when the resolution of the board of directors is passed. The call notice is drawn up and signed by the Secretary and it should contain particulars of the manner in which call is made. The amount of the call becoming due and also the total amount which would be paid up, upon such call being paid, on the shares, must also be given. The notice would be described as “First Call”, “Second Call” or “Final Call”, as the case may be. The Secretary should prepare a list of members, known as the *call-list*; a specimen of which is given below :—

CALL LIST

First Call of Rs. per share on ordinary shares due on

.

No.	Name	Address	No. of Shares	Folio	Amt. Due Rs.	Date Paid	Amt. Paid Rs.	Remark

The Call list is prepared from the Register of Members. The amount due from the members should be totalled and checked with the total amount due in respect of the call in order to ensure that there are no errors.

The next duty of the secretary is to issue *call letters* in accordance with the regulations of the Articles for the giving of notices to members, and a record of the posting of these letters should be

preserved for future reference. A Call letter is written somewhat as follows :—

Jiyajirao Cotton Mills Co. Ltd.

No.

Birla Nagar

.

Gwalior,

.

Nov. 15, 1953.

.....

Dear Sir/Madam,

I am directed to inform you that the directors by a resolution of the Board dated have made a call of Rs. per share on the shares of the company, making these shares fully paid/paid up to the extent of Rs. per share.

The amount due from you in respect of the shares registered in your name is Rs. which amount must be sent on or before together with this entire notice, to the company's bankers, ... Bank Ltd. Gwalior or to any branch of the Bank, which will return the notice duly receipted

The Call Letter, when duly receipted, should be carefully preserved, as it will have to be surrendered subsequently when the share certificates are issued, and a further communication in this connection will be sent to you in due course.

Your faithfully,

for Co. Ltd.

.

Secretary

The Call money may be paid by the shareholders either directly at the company's office, or through the company's bankers. When the amounts are paid, they are credited in the shareholders' accounts in the share ledger.

Forfeiture of shares :

The shares on which call money remains unpaid, may after proper notices be forfeited. The law in this connection has already been discussed in Book I. It may, however, be pointed out that in the case of forfeiture a resolution must be validly passed at a properly constituted meeting, and a copy thereof be sent to the member concerned. The following is a specimen of such a resolution :—

"RESOLVED that shares of Rs. each numbered inclusive, whereupon Rs. a share has been paid and which at the date of this resolution were standing in the name of Mr. of who, has failed to comply with the notice served upon him dated the be, and they

are hereby forfeited for non—payment of the final call of Rs. a share made on the and for non-payment of interest thereon, and that the said shares be disposed of as the director think fit in the best interests of the company”

Re-issue of forfeited shares :

Similarly, in the case of re-issue of forfeited shares, in order to vest the shares in the purchaser, the directors should pass a resolution in the following form :—

“RESOLVED that shares of Rs. , Rs. per share paid up, numbered inclusive, having been duly forfeited by a resolution of the Board dated be reissued to Shri of as fully paid, at Rs. per share, representing the unpaid final call of Rs. per share any Rs. per share premium, that the seal of the company be affixed to the transfer of the said shares to the said Sri ; that the said transfer be and is hereby passed for registration; and that a certificate for the shares in the name of, Sri be duly sealed and signed.

SHARE CERTIFICATES

A share certificate is a document of title (sec 29) which is issued by a company to every shareholder. The following is a specimen of share certificate :—

Specimen of Share Certificate

Counterfoil No. Dated 195 Name Shares Nos. to Certificate sent to per post Dated Register folio	No. No. of Shares Co. Ltd. This is to certify that Mr. of is the registered holder of share fully paid of Rs. each, numbered to inclusive, subject to the rules and regulations of the country. Given under the common Seal of the company this day 195 } Directors } Secretary
---	---

COMPANY SECRETARIAL PRACTICE [243]

According to section 108, share certificates must be ready for delivery within 3 months after allotment or after registration of a transfer, unless the terms of issue provide otherwise. After the certificates are ready, the shareholders have to be advised that they are ready for delivery in exchange for allotment letters. Usually a notice is sent to them, which is worded as follows :—

Jiyajeerao Cotton Mills Co Ltd.

Birlanagar,
Gwalior,
26 Jan., 1952.

Dear Sir/Madam,

I have to inform you that share certificates are now ready for both and shares. They will be exchanged for the Application, Allotment and First and Second call receipts given to you by the company's bankers for the different instalments paid by you. If you are unable to attend at this office personally to effect the exchange above mentioned, please fill in, sign and forward to me, one of the two forms appended hereto.

Yours faithfully,

To

for Co. Ltd.
Secretary.

To

The Secretary,

. Co. Ltd.,
.

Place

.
Date

Sir,

I enclose herewith receipts representing the full amount of the instalments paid upon the ordinary and/or preference shares standing in my name, and I hereby request you to forward the share certificates in respect of same to this address, at my risk.

Yours faithfully,

Place ..
Date

To
The Secretary,
.. Co. Ltd ,

Sir,

Kindly hand my share certificate to Mr. of ,
who will hand you the allotment letters and banker's receipt in
exchange. Their receipt for the said certificate shall be
your full discharge.

Yours faithfully,

In case a share certificate is lost, a public notice of the loss of
the certificate is required to be given in the news-papers, the cost of
which is borne by the shareholder. The following is a specimen of
such a notice :—

PUBLIC NOTICE

Jiyajeerao Cotton Mills Co. Ltd.

Notice is hereby given that an application has been made to
the Directors of this company for the issue of a duplicate share
certificate in respect of to standing in the name
of Mr. of on the statement that the original
certificate has been lost. If no objection is received within a month
from this date, the directors will proceed to deal with this
application.

Date :

By order of the Board,

Secretary

The following are the circumstances in which a company
issues share certificates :—

- 1 In exchange for letters of allotment and cash receipts, if
any, when shares are offered to the public.
2. On the registration of a transfer of shares.
3. In respect of shares acquired by a person in consequence
of the death or insolvency of a member.
4. In exchange for a worn out or defaced share certificate.
5. In respect of a share certificate which has been lost,
mislaid, destroyed or stolen.
6. When a share certificate is to split up

Note : The subject of "transfer and transmission of shares"
has already been discussed in Book I, hence it is not repeated here.

CHAPTER III

STATUTORY BOOKS & ACCOUNTS

Every company is required to maintain the following books, and it is the duty of the Secretary to see that they are properly kept :—

1. Register of Members :—

According to sec. 31, every company must keep a register of its members containing the following particulars :—

- (i) Names addresses and occupations of the members ;
- (ii) Number of shares held by each member and the distinctive members of such shares ;
- (iii) The amount paid or regard to be considered as paid on the shares of each member ;
- (iv) The date at which each person was entered in the register as a member ;
- (v) The date at which any persons ceased to be a member.

Index of members :

Under sec. 31 A (1), every company having more than 50 members should also keep an index of the names of the members of the company and must within 14 days after the date on which any alteration is made in the register of members make any necessary alteration in the index. The index may be in the form of a card index, but it must contain sufficient indication to enable the account of any particular member in the register to be readily found. If default is made in complying with these provisions, the company and every officer of the company who is knowingly and willfully in default, shall be liable to a fine not exceeding Rs. 50/-

Inspections and copies of register :—

Under sec 36 (1), the Register of Members and the Index of Members must be kept at the registered office of the company. Every member is entitled, free of charge, to inspect the register and the index and to make extracts therefrom. An outsider can inspect these on payment of fee not exceeding Re 1/-. Copies of the Register or any part thereof can be demanded by any person, whether member or not, on payment of -/6/- for every 100 words or fraction thereof. It is the duty of the secretary to send the copy to the applicant within 10 days.

Rectification of register :

Section 38 provides that —If—(a) the name of any person is fraudulently or without sufficient cause entered in or omitted from

(b) default is made or unnecessary delay takes place in entering on the register the fact of any person having ceased to be a member ;

The aggrieved person or any member of the company can apply to the Court rectification of the register.

The Court may either refuse the application or may order rectification of the register.

No trust to be entered :

The Register of Members, under section 32, must contain, in a separate part, a list of members and summary of capital. This register is the creditors' guarantee showing them to whom and to what they have to trust and must, therefore, be properly kept.

According to section 33, no notice of any trust, expressed, implied or constructive shall be entered on the register or be receivable by the register. It means that the persons whose names appear on the register as the holders of shares may be treated in all ways as the beneficial owners by the company.

Closing the register :

Under sec. 37, a company may on giving 7 days previous notice by advertisement in some newspaper circulating in the district in which the registered office of the company is situated, close the register of members for any time or times not exceeding in the whole 45 days in each year, but not exceeding 30 days at a time. The register has to be closed :—

- (i) When dividend warrants are written up ;
- (ii) When the annual return is prepared ;
- (iii) When further shares are offered to existing members pro rate ; or
- (iv) When the share capital is reconstructed.

British Register :

Under sec. 41, a company having a share capital may if authorised by its register of the members called the British Register. It is deemed to be a part of the company's principal register of members. A copy of every entry made in the British Register must be transmitted to the company's registered office in India for being recorded in the duplicate of the British register to be kept as part of the principal register.

This annual list must also contain a summary distinguishing shares issued for cash and those issued for any other consideration, and must specify the undermentioned particulars :—

1. The amount of the share capital and the number of shares into which it is divided.
2. The number of shares taken from the commencement of the company up to the date of the return.
3. The amount called up on each share.
4. The total amount of calls received.
5. The total amount of commission in respect of shares or of debentures.
7. The total number of shares forfeited.
8. The total amount of shares or stock for which share warrants are outstanding.
9. The total amount of share warrants issued and surrendered respectively since the date of the last return.
10. The number of shares or amount of stock comprised in each share warrant.
11. The names and addresses of directors, managers or managing agents and the changes in their personnel since the last return with the dates of the changes; and
12. The total amount of debt due from the company in respect of all mortgages and charges required to be registered with the Registrar.

The above list and summary is known as *annual return* and must be completed within 21 days from the first or only ordinary general meeting in the year; and a copy thereof duly signed by the director or the secretary, with a certificate as to its correctness, must be filed with the Registrar. It is as follows :—

I, ... do hereby certify that the above list and summary, truly and correctly states the fact as they stood on day of . . . 195—.

Secretary

3. Minute Books :

Under section 83, every company is required to keep minutes of all proceedings of general meetings and of its directors to be entered in books kept for that purpose. Any such minute, if signed by the chairman of the meeting at which the proceedings were had, or by the chairman of the next succeeding meeting, shall be evidence of the proceedings.

The books containing the minutes of proceedings of any general meeting of a company must be kept at the registered office of the company and they shall remain open to the inspection of any member free of charge during business hours subject to reasonable restrictions so that at least two hours in each day are allowed for inspection. Any member can, at any time after 7 days from the meeting, demand a copy of the minutes, which must be supplied to him with seven days after he has made the request in that behalf. The Minute Books of the Directors and shareholders can be inspected by the auditors at any time.

It should also be noted that separate minutes books should be kept for recording the proceedings of general meetings and board meetings. It is because the general meetings are open to the inspection of the members of the company, whereas the minutes of board meetings cannot be touched by them.

4 Register of Directors, Managers Etc. : —

According to section 87, every company is required to keep at its registered office a register of its directors, managers and managing agents containing the following particulars :—

(a) In the case of an individual, his present name in full, any former name or surname in full, his usual residential address, his nationality, his business occupation and particulars of other directorship, if any.

(b) In the case of a corporation, its corporate name and registered or principal office, and the full name and nationality of each of its directors ; and

(c) In the case of a firm, the full name, address and nationality of each partner, and the date on which each became a partner.

Further, the company must within 14 days from the appointment of first directors and within 14 days of a change among its directors, etc. or in any of the particulars contained in the register, send to the Registrar a return in the prescribed form containing the particulars specified in the register.

This register should be kept open to the inspection of any outsider on payment of the fee not exceeding R 1/- during business hours, for at least two hours in each day.

5. Register of Contracts :—

Under sec. 91-A (3), every company must keep a register of all contracts or arrangements in which the directors are directly

or indirectly interested. Such a register should remain open to inspection by any member of the company at the registered office of the company during business hours.

6. Register of Mortgages and charges :—

According to section 123, every company is required to keep a register of mortgages and enter therein all mortgages and charges specifically affecting property of the company and all floating charges on the undertaking or on any property of the company, giving in each case a short description of the property mortgaged or charged, the amount of the mortgage or charge and (except in the case of securities to bearer) the names of the mortgages or persons entitled thereto.

If any director, manager or other officer of the company knowingly and wilfully authorises or permits the omission of any entry required to be made in pursuance of the above section, he shall be liable to a fine not exceeding Rs. 500/-

7. Register of Debenture Holders :

It is not legally compulsory for a company to maintain a register of debenture-holders; but it is usually kept by the companies issuing debentures. According to sec. 125, it should remain open to the inspection of the debenture-holders except when it is closed in accordance with the articles.

8. Books of Account :—

According to section 13, every company should keep proper books of account with respect to :—

- (i) all sums of money received and expended by the company and the matters in respect of which the receipt and expenditure takes place ;
- (ii) all sales and purchases of goods by the company ;
- (iii) the assets and liabilities of the company.

These books of account should be kept at the registered office of the company or at such other place as the directors think fit and should remain open to inspection by the directors during business hours.

Where a company has a branch office ; proper books of account relating the transactions effected at the branch may be kept at the branch office ; but proper summarised returns, made up-to-dates at intervals of not more than two months, must be sent

by the branch office to the head office for incorporation in the principal books of account.

The books of account are open to inspection by the directors during business hours; and under compulsory regulation 105 of Table-A, the members are also entitled by a resolution passed in general meeting to inspect the books of account.

As regards books and accounts the secretary's individuality and knowledge will greatly influence the keeping of accounts as a whole. It may also be remarked here that it is the duty of the secretary to keep the directors fully informed with regard to the true financial position of the business from time to time. He should submit a financial statement at each meeting of the Board of Directors. Proper lists of company's debtors and creditors should also accompany the financial statement. He should also keep the Board thoroughly informed from time to time with actual reports made of the work done by the business and submitting periodical returns of the same.

9. Annual Accounts :—

Under sections 131 (1) and (3) and 184, the directors of every public company are required :—

- (i) To send the members and debentures holders ;
- (ii) To lay before the annual general meeting of members; and
- (iii) To file with the Registrar of Joint Stock Companies—

In each Calendar year a balance sheet and a profit and loss account or an income and expenditure account in the case of a company not trading for profit. The account are to be audited and must be presented not later than 18 months after the incorporation of the company, and thereafter once in every calendar year.

Balance sheets its contents etc. :

According to section 132 (1), the balance sheet should contain a summary of the property and assets, and of the capital and liabilities of the company, giving such particulars as will disclose the general nature of those assets and liabilities and stating how the value of the fixed assets has been arrived at.

Under sub. sec. 2 of sec. 132, the balance sheet should be in form marked F in the Third Shedule or as near thereto as circumstances admit.

When a company has issued shares at a discount under sec. 105-A, every subsequent balance sheet must contain particulars

of the discount allowed on the issue of the shares or of so much of that discount as has not been written off at the date of the balance sheet.

According to section 105B, every company issuing redeemable preference shares must include a statement in its balance sheet specifying what part of the issued capital of the company consists of such shares and the date on or before which those shares are liable to be redeemed. Further, according to section 106, where a company has paid any sums by way of commission in respect of any shares or debentures or allowed any sums by way of discount in respect of any debentures, the total amount so paid or allowed or so much thereof has been written off.

Under section 131-A, there must be attached to every balance-sheet a report (known as the Director's Report) with respect to the state of the company's affairs, clearing showing the amount, if any, which they recommended by way dividend and the amount, if any, which they propose to carry to various reserves.

Under section 132-A there should be annexed to the balance-sheet of a holding company other than an investment company—

- (i) the last audited balance-sheet, P. & L a/c auditors' report of each subsidiary and sub-subsidiary company, and
- (ii) a statement showing how the aggregate profits and losses of the subsidiary companies have been dealt with in accounts of the holding company.

Profit and Loss Account its contents :

As regards the contents of a profit and loss account, the compulsory regulation 107 of Table A provides as follows :—

- (1) The P. & L a/c shall show, arranged under the most convenient heads, the amount of gross income distinguishing the several sources from which it has been derived ;
- (2) The P. & L. a/c shall show, arranged under the most convenient heads, the amount of gross expenditure distinguishing the expenses of the establishment, salaries and other like matters ;
- (3) Every item of expenditure fairly chargeable against the year's income shall be brought into account so that a just balance of profit and loss may be laid before the meeting ; and

(4) Where any expenditure has been incurred during the years, which may in fairness be distributed over several years, the whole amount of such expenditure must be stated in the P. & L. a/c together with the reason why only a portion thereof is charged against the income of the year, unless the company has decided otherwise in general meeting.

Again, section 132 (3), in this connection, provides as below :-

(1) That the directors' remuneration, the managing agents' remuneration and the amount of depreciation shall be shown as separate items in the P. & C. a/c ; and

(2) Where any director is nominated by a company as a director of some other company, any remuneration received by such director from that other company must be shown in the P. & L. a/c of the company by way of footnote or in a statement attached thereto.

CHAPTER IV

COMPANY RESOLUTIONS.

Meaning of a resolution :

Any proposal, when adopted by the meeting, becomes a resolution.

Kind of resolutions :

There are three kinds of resolutions, viz.,

(i) Ordinary, (ii) Extra-ordinary and (iii) Special.

1. Ordinary Resolution :

The Indian Companies Act does not define an ordinary resolution, but indirectly it has been referred to as a 'resolution passed by a company in general meeting in person or by proxy (where proxies are allowed) and entitled to vote.

Business transacted :

Such a resolution is used for ordinary routine business at general meetings, but it can also be used for special business, e. g. alteration of capital under sec. 50, unless the Act or the Articles of the Company demand an extra-ordinary or special resolution

2. Extra-Ordinary Resolution :

According to section 81 (1), an extra-ordinary resolution is one which is passed by a majority of not less than $\frac{3}{4}$ of such members entitled to vote as are present in person or by proxy at a general meeting of which notice to propose the resolution as an extra-ordinary resolution has been duly given. When all the members of a company are present and vote for the resolution, it will be valid to pass an extra-ordinary resolution inspite of any defect in procedure.

Cases in which extra-ordinary resolution is necessary :

(1) To remove a director whose period of office is liable to determination at any time by retirement of directors in rotation (sec. 86—G).

(2) To wind up voluntarily when the company cannot by reason of its liabilities continue its business (sec. 208).

(3) To sanction an arrangement between a company and its creditors and to sanction certain acts to be done by the liquidator in a voluntary winding up (section 212).

(4) To carry out any specified purpose provided for in the articles of the company.

3. Special Resolution :

According to section 81 (2), a special resolution is one which is passed by a majority of not less than $\frac{3}{4}$ (as in the case of an extra-ordinary resolution) at a general meeting of which not less than 21 days notice, specifying the intention to propose a resolution as a special resolution, has been duly given.

The main point of distinction between a special and an extra-ordinary resolution lies in the *length of notice*; but if all the members who are entitled to vote be present and agree, a special resolution may be passed at less notice than 21 days.

Cases in which special resolutions are necessary :

- (1) To change the name of the company [Section 11 (4)].
- (2) To Change the place of the registered office of the company from one State to another (Section 12).
- (3) To alter the Memo. with respect to objects of the company (sec. 12).
- (4) To alter the articles of a company (sec. 20).
- (5) To reduce the share capital of the company (sec. 55).
- (6) To convert the existing liability on shares into a reserve liability (sec. 69).
- (7) To make liability of directors unlimited [sec. 71 (1)].
- (8) To assign the office of a director or a manager (sec. 82—B).
- (9) To sanction additional remuneration of the managing agent [sec. 87—C (1)].
- (10) To appoint inspectors to investigate company's affairs [Sec. 142 (1)].
- (11) To procure a winding up by the court (sec. 162).
- (12) To wind up a company voluntarily [sec. 203 (2)].
- (13) To confer power on liquidator in a voluntary winding up of a company for entering into any arrangement for sale with a transferee's company and accept shares etc. of the transferee's company as consideration for the sale of the property of the transferor's company (sec. 208—C).

(14) To substitute memorandum and Articles for deed of settlement under sec. 267.

Registration and copies of resolutions :

A printed or typed copy of every extra-ordinary and special resolution duly certified under the signature of an officer of the company must be filed with the registrar within 15 days of the passing of the resolution.

Where articles have been registered, a copy of every special resolution for the time being in force must be embodied in or annexed to every of the articles issued after the passing of the resolution. But where articles have not been registered, a copy of every such resolution must be forwarded to any member at his request, on payment not exceeding Re. 1/- In case of default, the company and every officer (who is in default), shall be liable to a fine not exceeding Rs. 20/- for each day so long as the default continues. It should, however, be noted that for not embodying or annexing a copy of special resolution to the articles, the fine does not exceed Rs. 10/- only.

Note : There is one more class of resolution, which require special majorities, e. g , as provided in sec. 153.

by them respectively. This list of members should be made available for the inspection of the members during the continuation of the meeting.

5. The secretary will thereafter read the notice convening the meeting and exhibit the list of members for inspection.

6. He will also record the proceedings of the meeting and will take necessary action on the resolutions that may be passed in that meeting.

Ordinary General Meeting :

Section 76 of the Act makes it obligatory for a company to hold its first general meeting within 18 months from the date of its incorporation and thereafter once atleast in every calender year and at intervals of not more than 15 months after the holding of the last proceeding of the general meeting. The word 'Calender Year' referred to above, means a year commencing the 1st January and ending with 31st December. An ordinary general meeting is a meeting of the shareholders held after proper notice.

If default is made in complying with these provisions, a fine not exceeding Rs. 500/- may be levied on a director or manager who is knowingly a party to the default, and member, may call or direct the calling of a general meeting.

Business Transacted :

The business transacted at an ordinary general meeting may be either ordinary or both ordinary as well as special. The ordinary business consists of :—

1. Consideration of the company's audited accounts, viz', Profit and Loss A/C, Balance Sheet, auditors' Report and the Director' Report;
2. Declaration of Dividends;
3. Election of directors;
4. Appointment of auditors.

All other business that may be transacted at a company meeting is known as special business.

It is at this meeting that the shareholder are entitled to express their views as regards the management and other affairs of the company and to put questions to the directors and elicit from them such information and elucidation as to the working of the company as they may require.

Who may convene such meeting :

(1) Usually the articles provide for the calling of the ordinary general meeting of the company by the directors.

(2) Two or more members holding not less than 1/10th of the total share capital paid up or if the company has not a share capital, not less than 5% in number of the members of the company may call such a meeting. (Section 79 subsection 2 clause (a)).

(3) Sub-section 3 of Section 79 of the Act empowers the court to convene a meeting of a company, either on its own notion or on the application of any director of the company or of any member of the company entitled to vote thereat, when it is otherwise impracticable to call a meeting of the company in any manner in which meetings of that company may be called or to conduct the meeting of the company in manner prescribed by the Act or the articles.

Secretary's duties in connection with ordinary general meetings :

The various duties of a Company's Secretary in connection with General Meetings may be summarised as below :—

Prior the meeting :

Before the actual commencement of the meeting the secretary should do the following things :—

- (1) Arrange for the necessary accommodation for the meeting;
- (2) Prepare the agenda and get it approved by the chairman;
- (3) Assist the chairman in the drafting of his speech;
- (4) Arrange the necessary papers concerning the agenda of the meeting;

(5) All reports to be presented to the meeting must be made ready;

(6) Issue a reminder to every director two days before the meeting to ensure their attendance at the meeting (this is customary);

(7) After the accounts of the company have been audited and the auditors' report received, the secretary should put the company's audited accounts before the directors for the appropriation of profits and should help him in the preparation of the Directors' Report. He should get it approved and signed by them;

(8) The Secretary should arrange for the printing of audited accounts and the Various reports;

(9) The Secretary should also arrange for sending the final accounts atleast 14 days prior to the date of the meeting to every member and also to those other persons who, under Section 146, are entitled to receive them (e. g., Debentureholders and debenture trustees);

(10) A Copy of the final accounts must also be deposited at the registered office of the company for the inspection of the members during a period of atleast fourteen days prior to the meeting. If there are foreign shareholders also, a copy of the notice convening the meeting must be advertised in some newspapers and must also be put up on a notice board at the registered office of the company.

(11) The secretary should also close the share books of the company for the purpose of balancing the register of members, writing up dividend lists and dividend warrants and preparing the annual returns;

(12) The Secretary should also make the necessary arrangements for dealing with the proxies, which must be scrutinised to ascertain that they are in order;

(13) When it is anticipated that a poll may be demanded, preparation should be made for polling.

At the meeting :

(1) To attend the meeting in good time and to arrange for the proper supplies of stationary;

(2) Keep record of attendance;

(3) Keep available the following :—

- (a) Copies of memorandum and articles;
- (b) Copies of final accounts and reports;
- (c) All proxies lodged and list thereof;
- (d) Register of Members;
- (e) Minute books;
- (f) Ruled sheets for use, if a poll is demanded;

(4) Take accurate and efficient notes of the proceedings of all resolutions passed at the meeting;

(5) Assist the chairman in every possible way particularly in seeing that the meeting is properly constituted.

Post to the meeting :

(1) When the meeting is over, the secretary should prepare the minutes of the meeting.

(2) Then after he should take action on the points arising from the meeting such as writing letters, despatching allotment letters, informing the persons elected as directors and auditors etc.

(3) After the audited accounts have been laid before the ordinary general meeting, three copies thereof signed by the secretary must be filed with the Registrar. If the accounts have not been adopted by the meeting, a statement of this fact along with the reasons therefor must be annexed to the accounts;

(4) The annual return must be completed within 21 days from the date of the meeting, signed by the secretary and filed with the Registrar.

Extra ordinary general meeting :

Besides the ordinary general meeting other general meetings may be held according to the exigencies of the business of the company from time to time and they are known as extra-ordinary general meeting, at which only special business, notice whereof has been duly given beforehand, can be transacted. The articles of a company almost invariably provide that all other meetings, except the annual general meetings, which are otherwise known as ordinary general meetings, shall be called extra-ordinary.

Who may convene such meetings :

Extra ordinary general meetings may be called in three ways :—

(1) **BY THE DIRECTORS**—The directors of a company may on their own initiative call an extra ordinary general meeting in accordance with the provisions of the articles, whenever such a meeting is deemed necessary.

(2) **BY THE DIRECTORS UPON SHAREHOLDERS' REQUISITION**—According to section 79, the directors may call an extra ordinary meeting upon the shareholders' requisition mentioning the object of the meeting, provided the requisitioning shareholders hold not less than one tenth of the issued capital on which there are no calls in arrears. Such meeting should be convened within 21 days from the date of the requisition.

(3) **BY THE REQUISITIONING SHAREHOLDERS**—If the directors fail to comply with the requisition within 21 days, the requisitioning members themselves call a meeting. It should however, be noted that the requisitionists can do so within 3 months from the date of the deposit of the requisition and they will be

entitled to recover any reasonable expenses incurred in calling the meeting from the company, which in its turn can claim the same from the defaulting directors.

The special business to be transacted at an extra ordinary general meeting, requires an extra ordinary or a special resolution. Because at an extra ordinary meeting some special business is transacted, it is usual to prepare a circular explaining in detail the nature of the special business, and send it along with the notice to the members so that they may know beforehand why the meeting is being called and also decide whether or not to attend the meeting.

Secretary's duties in connection with extra ordinary general meetings :

It may be pointed out here that the secretary's duties in this connection are more or less identical with his duties at an ordinary general meetings with such additional duties as may be required on account of the special business for which a particular extra ordinary general meeting is called. However, he should give attention to the matters noted below :—

(1) Draft any circular which may have to accompany the notice of the meeting and have it approved by the chairman before it is actually issued to the members;

(2) The notice must also state that special business for which the meeting is being called and that it is the intention to propose the resolution as an extra ordinary or special resolution as the case may be;

(3) If an extra ordinary or a special resolution has been passed at the meeting, a copy of the same should be filed with the Registrar within 15 days.

Board meeting :

Legally speaking, the management of a company vests in its directors and the ordinary business of joint stock companies is usually transacted by the directors, who meet together for the transaction of the company's business at, what are called, board meetings. The exact nature of business to be transacted at Board's meetings depends upon the articles of association. However, there are certain matters which can be dealt with only at board meetings e. g., allotment of shares, making of calls, forfeiture of shares, issue of debentures, appropriation of profits etc.

Board meetings are held periodically. Usually the directors are empowered by the articles to transact business either by meetings or by correspondence.

Secretary's duties in connection with board meetings :

(1) Prepare an agenda and issue notice of the meeting to the directors.

(2) Arrange for the attendance of directors and other officers, e. g., auditors, legal advisers etc;

(3) Keep ready all the documents that may be required at the Board meeting;

(4) See that the board room is well equipped and arranged;

(5) Read the minutes of the previous meetings and explain how far the matters arising therefrom have been given effect to.

(6) Produce the necessary documents for inspection, approval or signature of directors;

(7) Take notes of the proceedings at the meeting;

(8) Write the minutes of the proceedings of the meeting and to carry out the orders of the board.

CHAPTER VI

COMPANY MEETINGS (Contd.)

Introduction :

The procedure to be followed at company meetings is usually governed by the Articles, but the Indian Companies' Act has also made certain provisions in order to check undesirable practices in the conduct of joint stock company meetings, and they are contained in section 79 (1) and Regulations 56, 66, and 112-116 of Table A.

NOTICES OF MEETINGS

Period of notice :

In order to constitute a valid meeting, it must be convened by a proper notice. As a general rule, all meetings of a public company and of a private company which is the subsidiary of a public company, other than a meeting for the passing of a special resolution, are to be called by not less than 14 day's notice in writing. A private company which is not a subsidiary of a public company, may, however, prescribe a shorter notice for the purpose of convening an ordinary or extra-ordinary general meeting. Where it is intended to pass a special resolution at a general meeting, the period of notice is to be 21 days. In either case, however, the general meeting may be convened by a shorter notice with the consent of all the members entitled to receive notice of the meeting.

Nature of notice :

The general rule in this connection is that a notice of a general meeting must give a sufficiently frank and full disclosure to the shareholders of the facts upon which they are asked to vote. A notice must clearly specify the special business which is to be transacted at the meeting to which it relates. The notice must be adequate and state clearly the place, day and time of meeting. It must disclose all facts necessary to enable the shareholders receiving it to determine whether or not they ought to attend the meeting.

Mode of giving notice :

The company secretary is particularly responsible for the due despatch of notices. The rules as to the issue and service of notices of general meeting of a company (including a private

company are contained in the compulsory regulations 112 to 116 of Table A. Regulations 112 provides that a notice may be given to any member either personally or by sending it by post to him to his registered address or (if he has no registered address in India) to the address, if any, within India supplied by him to the company for the giving of notices to him. According to regulation 113, if a member has no registered address in India, and has not supplied to the company an address in India for the giving of notices to him, a notice addressed to him and advertised in a newspaper circulating in the neighbourhood of the registered office of the company shall be deemed to be duly given to him on the day on which the advertisement appears.

Under regulation 114 a notice may be given by the company to the joint holders of a share by giving the notice to the joint holder named first in the register in respect of the share.

Under regulation 115, a notice may be given by the company to the persons entitled to a share in consequence of the death or insolvency of a member by sending it through the post in a prepaid letter addressed to them by name, or by the title of representatives of the deceased or assignee of the insolvent or by any similar description at the address supplied for the purpose by the person claiming to be so entitled, or (until such an address has been so supplied) by giving the notice in any manner in which the same might have been given if the death or insolvency had not occurred.

According to regulation 116, notice of every general meeting must be given to every member of the company (including bearers of share warrants except those members who (having no registered address in India) have not supplied to the company an address within India for the giving of notices to them. Notice must also be given to every person entitled to a share in consequence of the death or insolvency of a member, who but for this death or insolvency would be entitled to receive notice of the meeting.

Extent of amendment to be moved :

The general rule is that no amendment can be removed at a general meeting which goes beyond the matter specified in the notice. The same view has been enunciated by Blagden, J., as follows :—"I understand the general rule on the point to this—first, the amendment must be germane to the subject-matter of the proposition, and, secondly, that they must not be, in substance, a direct negative of it. If, for an example, a resolution were that a

particular piece of business be now considered it would be in substance a direct negative to move that it be considered 999 years hence."

Irregularities in notice :

The irregularities in the matter of notice, etc. can be waived by the shareholders, if the transactions to which they relate is not ultra vires, as an act which is within the power of the company can be ratified by all the members of the company without a formal meeting or by calling a meeting whereat such an irregularity can be set right by the members present thereat. An ultra vires cannot, however, be ratified even by the consent of all the members*

AGENDA

The term 'agenda' means a statement of the business to be transacted at a meeting, whether of the company or of the board. As a matter of fact an agenda is drawn up by the Secretary in consultation with the Chairman. It is merely indicative and should not be exhaustive.

PROXIES

Meaning of proxy :

A proxy is an instrument in writing authorising a person (who must be a member of the company unless the articles provide to the contrary) to vote for another shareholder at a certain general meeting or meetings of the company. In other words, it may be said that a proxy is a person who is authorised to attend and vote at a company meeting on behalf of another person.

The proxy must be in a form prescribed by the articles. It must be stamped and must be lodged at the office of the company within a prescribed time.

Form of proxy :

The form of proxy is usually given in the articles of a company; but if it is made in the form prescribed by Regulation 67 of Table A as noted below, it would not be questioned on the ground that it would not be questioned on the ground that it fails to comply with any special requirement specified for such instrument in the articles.

Proxy form according to regulation 67 :

FORM OF PROXY

.....Co., Ltd.,

'I.....of.....in the district of.....being a member of the.....company, Ltd., here by appoint.....of.....as

my proxy to vote for me and on my behalf at the ordinary or extra ordinary as the case may be, general meeting of the company to be held on the.....day of.....and at any adjournment thereof.

Signed this.....day of.....

Attestation and stamping of proxies :—

Usually proxies are required by the articles to be attested, i. e., to be signed in the presence of a witness or witnesses and where they are required to be attested as such, attestation becomes indispensable.

According to article 52 of the Indian Stamp Act, a proxy empowering another to vote at a general meeting must be stamped with an adhesive stamp of as. 2

Again, according to section 79 (2) (g), a proxy must be a member of the company unless otherwise provide in the articles. A proxy may in the instance be signed in blank and given with a blank left for the name of the person entitled to vote, and may be subsequently filled up by any person duly authorised to fill in the blank. Proxies not bearing the date of execution, if lodged within the time allowed and before the date of meeting, are valid.

Deposit of Proxy :

Compulsory regulation 66 of Table A provides that proxy forms must be deposited at the registered office of the company at least 72 hours before the time of holding a meeting. In view of this regulation, the proxies lodged after the date of the original meeting, but deposited before the specified time before the adjourned meeting, cannot be used for the purpose of voting at the adjourned meeting. It shall not be out of place to mention here that the appointment of a proxy, unless made irrevocable for valuable consideration, can be revoked. The revocation must conform to the provisions in the articles in this respect.

Statutory right of a company to appoint proxies :

Section 80 provides that a company, which is a member of another company may, by resolution of the directors, authorise any of its officials or any other person to act as its representative at any meeting of that other company, and the person so authorised shall be entitled to exercise the same powers on behalf of the company which he represents as if he were an individual shareholder of that other company.

Employment of company's funds by directors for obtaining proxies :

The directors may, provided that they are acting bonafide in the interests of the company in printing or sending out to the shareholders, proxy forms filled up with the names of the directors or their nominees as the proxies, and in stamping the forms or the envelopes in which to return them.

It is the duty of the company secretary to examine all the proxies lodged at the company's office, in order to ascertain that the document was received at least 72 hours prior to the holding of the meeting, that it is in proper form, attested and stamped, that it is properly signed, that the name of the member agrees with the Register of Members and that the person appointed is a member of the company—(Not in the case of a representative of a company shareholder). Further, the secretary should prepare a list showing the names of the members who have appointed proxies, the number of votes to which they are entitled and the names of persons who have been appointed proxies. These lists should be available for the use of the chairman. It may also be mentioned that sometimes the secretary is also required to send out with the notice of meeting stamped proxy forms and an invitation to the shareholders to appoint one of the directors to vote at the meeting on their behalf.

POLL**Meaning of poll :**

Usually voting at company meetings is carried out by show of hands on the principle of 'one man one vote'; but sometimes, it becomes necessary that the members of the company should be able to exercise voting power in proportion to their interest in the company, and in order to do so, voting is done by means of poll. On a poll, all actual available votes that the members present in person or by proxy may possess, are counted as distinguished from a mere counting of hands, on a show of hands of those present in person, as in the latter case, the persons present by proxy have no right to vote, unless the articles otherwise provide, while, on a poll votes may be given either personally or by proxy.

If a poll is duly demanded, the show of hands is nullified.

Statutory right to demand poll :

Members have the right, under the common law; to demand a poll on any motion before the meeting; but this right may be

qualified or excluded by the articles. According to Section 79 (1), in the case of a public company, five members present in person or by proxy or the chairman of the meeting or any member or members holding not less than one-tenth of the issued capital which carries voting right shall be entitled to demand a poll, while in the case of a private company, the right to demand a poll is given to one member, if not more than seven members are personally present in a meeting, and to two members, if more than seven members are personally present. For the purpose of demanding a poll, two joint holders may count as two, unless the articles otherwise provide.

Manner of taking a poll :

When a poll is demanded, the chairman must grant it and fix the time and place for taking it. The articles usually provide that the poll is to be taken in such manner as the chairman directs ; but it should be noted that the chairman possesses the discretion as to how and when the poll is to be taken. Accordingly, he may direct that the poll may be taken then and there or he may appoint a subsequent day for the purpose. The poll will be taken by every person who desires to vote, signing a paper headed, as the case may be, for or against the motion. The votes of each member are then inserted and these are added up, the proxies being also counted. Afterwards, the chairman declares the result.

It may also be remarked that the chairman of a general meeting has the power to decide all incidental questions that may arise at such meeting. He may appoint persons, if so authorised, to examine and count the votes at a poll. Such scrutineers may be appointed by the chairman of the meeting and report the result to the Chairman who alone has to declare it. If the articles allow a member to inspect the voting papers, the Court may, on strong grounds being shown and on being satisfied that the application for inspection is bonafide, give him an opportunity to do so, unless when it appears that such inspection would not yield any useful result.

VOTING

Manner of voting :

Usually the articles of a company prescribe the procedure to be observed in connection with voting at general meetings. The articles may also restrict the mode and manner of voting. In the absence of any specified provisions in the articles to the contrary,

every member present, who is entitled to vote, has one vote only irrespective of the fact that he also holds a proxy for an absentee. The right of vote of a shareholder is a right of property which he may exercise according to his sweet will. As a general rule no person except the holders of shares can vote at a meeting in respect thereof, but the articles may provide that the guardian or the committee of a lunatic or any person of unsound mind (who must be a member) may attend the meeting and vote thereat on his behalf either on a show of hands or on a poll. Sometimes the articles place a restriction on the right of voting on those members who have failed to pay calls which are presently payable by them.

After the chairman has put the resolution formally to vote, he then calls for a show of hands thus, "those who are in favour of the resolution, hold up one hand; those who are against it, hold up one hand." He then counts the number for and against the resolution and states the result. According to compulsory regulation 55 of the Table A, the Chairman's declaration that a resolution has been carried shall (unless a poll is demanded) be deemed conclusive evidence of the fact:

MINUTES

Minutes are the written record of the proceedings at meetings. Section 88 makes it compulsory for every company to keep minutes of all proceedings of general and directors' meeting in books kept for the purpose. These minutes are to be signed by the chairman of the meeting at which the proceedings were held and they form a conclusive evidence of the proceedings. It is the duty of the company secretary to prepare the minutes and for this purpose he must be present at all the meetings and take necessary notes. Minutes should always constitute a succinct record of the proceedings to which they relate.

The minutes shall be kept at the registered office. Under section 83, the minutes of general meetings of the company are opened to inspection of members, but the minutes of the directors' meetings are not.

CONDUCT OF BUSINESS AT MEETINGS

Quorum :

The word 'Quorum' stands for certain number of qualified persons who must be present at a meeting before any business can be validly transacted. Usually the quorum is fixed by the articles of a

company and unless so fixed, two members in the case of a private company and five members in any other case, personally present, shall form the quorum. [Section 78 subsection 2 (b)] Proxies are not counted in the quorum but the representative of a company shareholder is counted. The articles sometimes provide for a smaller or different quorum for some particular class of business or for separate meetings of a particular class of shareholders—this is allowed.

Chairman :

The appointment of the chairman of board of directors is usually made according to the provisions of the articles, but if the articles do not make any provision, section 79 (2) (c) automatically comes in operation, accordingly, in such a case, any member elected by the members present at a general meeting may be chairman thereof.

If the articles contain any express provision with regard to the conduct of meetings, those rules must be strictly followed but in the absence of appropriate regulations, the chairman must act fairly and to the best of his judgement.

Duties of chairman :

(1) The primary duty of a chairman is to preserve order and to see that the business at the meeting is properly and regularly conducted and to take care that the sense of the meeting is properly ascertained with regard to any question before it.

(2) The chairman has to decide the points of orders raised at the meeting and any other matter that may be raised thereat

(3) It is the duty of the chairman to see that his own appointment is in order and that the meeting is valid.

(4) He should see that the business is taken up according to the agenda, unless subsequently altered by the consent of the meeting,

(5) The chairman should provide reasonable opportunities to all the members to express the views.

(6) It is one of his important duties to protect the rights of minority.

(7) He should see that all business is within the scope of the meeting.

(8) It is the duty of the chairman to decide as to whether any further discussions should or should not be allowed on any

question under discussion at a meeting and as to whether a closure motion should be allowed to be moved.

(9) It is the duty of the chairman to put all proper amendments to the meeting.

(10) On a poll being demanded it is the duty of the chairman to grant it and fix the time and place for taking it.

(11) Last but not the least, it is customary for the chairman to make a speech in placing the final accounts and the directors' reports before the members for their consideration. Usually, a printed copy of the chairman's speech is made available for the information of those interested in the company.

The chairman's speech is a document of great significance. It is indeed a picture of the industry in which the company is engaged. The principal object of the speech is to give the annual figures their due perspective, to remove misapprehensions and to elucidate the causes which have brought them about. It may also be pointed out in this connection that in most of the cases, it is the secretary who drafts the chairman's speech or review.

Casting vote :

Usually the articles of a company entitle the chairman for a casting or second vote, if the votes of members on the two sides are equal. Regulation 58 of Table A, which runs as follows, provides for a casting vote :—"In case of an equality of votes, whether on a show of hands or on a poll, the chairman of the meeting at which the show of hands takes place, or at which the poll is demanded, shall be entitled to a second or casting vote." In the absence of express provision, the chairman has no casting vote. If the chairman does not exercise his casting vote or if he does not possess it, and the voting on the two sides is equal, the motion is deemed not carried.

Motion :

The term 'motion' means a proposition or a proposal put forward at a meeting for discussion and decision. There is difference between a motion and resolution. A motion is a mere proposal whereas a resolution is the formal declaration about the actual decision on the proposal by vote of the persons present at a meeting. That is why, a motion is sometimes described as 'a proposed resolution' or 'the question before the meeting.'

Motions should be in writing, signed by the proposers and handed to the chairman. Usually, they are seconded, but this

is not necessary except when the articles require it. A motion cannot be withdrawn without the leave of the meeting. Any other provisions of the articles in this regard must be strictly observed.

Amendment :

As is implied from this word, an amendment means the revision of the original motion under discussion—(i) either by the addition of certain words, or (ii) the deletion of certain words or (iii) a combination of both these methods. Just like motions, amendments should also be in writing, signed and handed to the chairman. An amendment must be relevant to the original motion ; must be formally moved before the main question is put to vote ; must not be a mere negative ; and must be within the scope of the notice. Amendments cannot be withdrawn without the permission of the meeting. It is the duty of the chairman to allow reasonable discussion on each amendment. If the amendment is carried, the original motion is accordingly revised and that revised motion becomes the substantive motion. Every member present at a meeting has a right to speak only once on each motion or amendment. The mover of an original motion has a right of reply on the debate. It may also be pointed out that the language used by a speaker must be courteous and should not be offensive or personal.

The closure :

If the discussion on the motions or amendments drags on and becomes too lengthy, any one who feels that the motion should be put to vote in order to avoid the wastage of time, may propose that 'the question be now put to vote'. If seconded, the chairman puts it to vote and if carried, no further discussion can be allowed. The principal object of moving a closure is not to shelve the main question, but to secure an immediate decision. The other name of a closure is 'Gag'.

The previous question :

'Previous question' is a means of interrupting the debate. When it is considered unwise to discuss any motion which is already seconded, one may move what is called 'the previous question.' The form in which it is put is, "that the question be not now put." When the previous question is seconded, the chairman puts it to meeting. No discussion is allowed and it takes precedence of all other motions. It should, however, be noted that the previous question cannot be put during discussion of the amendment, but

should be put after the amendment is passed and the substantive motion is before the meeting. If it is carried the original motion is shelved once for all and if it is not carried, the original motion is put to the meeting without any further discussion.

Dilatory motion :

Previous question is one of the dilatory motions which are moved with the object to interrupt or adjourn the discussion. They may take the following other forms :—

'Next business' :

The object of this motion is to prevent a decision from being taken on the main question, and can be moved even when an amendment is being discussed. It is put in this form, 'that the meeting pass on to the next business'. After it is moved and seconded, it is put to vote. If it is carried, the original motion is disposed of ; but if it is lost, the debate continues.

Adjournment :

An adjournment may be moved to adjourn the meeting or the debate and its form is as below :—"That this meeting be now adjourned." Such a motion should clearly state for how long the meeting is to be adjourned and the date on which the adjourned meeting is to take place. The chairman on his own motion can adjourn the meeting, of course, with the consent of the meeting.

Disorder :

Sometimes the meeting is interrupted by the disorderly conduct of some members present. If the disorder persists, the meeting may be adjourned for a short time in order that the members in the mean time may make up their differences and come to an understanding.

Postponement :

A postponement usually arises when it is desired to obtain some additional information on the motion. The form of the motion will be :—"that further consideration of the motion be postponed until....." The mover of the original motion has a right to reply after which it is put to vote. If carried, the debate is put off ; but if lost, debate is continued.

SPECIMEN NOTICES

Statutory meeting :

Jiyajee Rao Cotton Mills Ltd.

Birla Nagar,

Gwalior.

Dated : 195 .

Notice is hereby given that pursuant to Section 77 of the Companies Act, the Statutory Meeting of the Company shall be held at.....on.....day, the.....day of.....195..... at.....O'clock in the.....noon.

By the order of the Board,

.....

Secretary.

Annual General Meeting :

Jiyajee Rao Cotton Mills Ltd.

Notice

Notice is hereby given that the thirty-second Ordinary General Meeting of the Jiyajee Rao Cotton Mills Limited, will be held at the Registered Office of the Company, Birla House, Birla Nagar, Gwalior, on Thursday, the 20th July, 1952, at 4 P. M. (S. T.) to transact the following business :—

1. To receive and adopt the Statement of Accounts for the year ended 31st March, 1952, and the Reports of the Directors and Auditors, and to declare dividends.

2. To elect a Director in place of Mr. Sahai who retires in accordance with Article 127 of the Company's Articles of Association, but is eligible for re-election.

3. To elect a Director in place of Mr. Rao who retires in accordance with Article 127 of the company's Articles of Association but is eligible for re-election.

4. To elect a Director in place of Mr. G. D. Birla who retires in accordance with Articles 127 of the Company's Articles of Association, but is eligible for re-election.

5. To elect a Director in place of Mr. B. M. Birla who retires in accordance with Article 126 of the Company's Articles of Association, but is eligible for re-election.

6. To appoint auditors for the current year and to fix their remuneration.

The Transfer Books of the Company will be closed from Friday, the 30th June, 1952 to Thursday, the 18th July, 1952, both days inclusive.

By Order of the Board,
Jiyajee Rao Cotton Mills Ltd.
Manager
.....
Director.

Gwalior, 19th June, 1952.

Extraordinary general meeting :

Jiyajee Rao Cotton Mills Limited

Notice is hereby given that an *extraordinary general meeting* of the company will be held at the Registered Office of the company, Birla House, Birla Nagar, Gwalior, on Monday, the 12th March 1953 at 4.30 P. M (S. T.) for the purpose of considering and if thought fit, of passing the following resolution as Extraordinary Resolution.

That the share capital of the company be increased by the creation of 20,000 ordinary shares of Rs. 10/- each to rank in all respects *pari passu* with the company's original ordinary share capital.

By Order of the Board.
.....
Secretary.

SPECIMEN AGENDA

Agenda for the annual meeting :

Held.....on.....19.....

AGENDA

1. The Secretary will read the notice convening the meeting.
2. The Chairman will propose that the directors' report and the balance sheet as at.....19....., be taken as read.
3. The Secretary will read the auditor's report.
4. The Chairman will address the meeting reviewing the year's activities and results, and the company's prospectus.
5. The Chairman will move the adoption of the report and accounts.
6. The Chairman will call upon a shareholder to second the motion, and will then invite discussion.

7. The Chairman will reply to questions and put the motion to the meeting and declare the result.
8. The meeting will elect directors.
9. The Chairman will move that the dividends recommended by the Directors in their report be declared. This, when seconded, will be put to the meeting, and the Chairman will declare the result.
10. The meeting will appoint the auditors.
11. A Vote of thanks to the Chairman will be moved.
12. The Chairman will declare the meeting closed.

Agenda for the first meeting of the Board :

Held at on 195.....

1. Certification of Incorporation;
2. Appointment of Managing Agents,
3. Appointment of Bankers;
4. Appointment of Auditors;
5. Company's Common Seal;
6. Agreement with Vendors;
7. Underwriting of Shares, and
8. Draft Prospectus.

Agenda for a subsequent Board meeting :

Held at on 195.....

1. Minutes of Previous meeting;
2. Resignation of Mr. K. Sahai a director;
3. Appointment of Director to fill casual vacancy;
4. Report of Transfer Committee;
5. Purchase of additional machinery;
6. Investment of Reserve Fund,
7. Declaration of an interim dividend,
8. Appointment of a Committee of the Board;
9. Any other business with the permission of the Chairman.

SPECIMEN MINUTES

Minutes of the statutory meetings :

Jiyajee Rao Cotton Mills Ltd.

MINUTES of the Statutory Meeting of the company held at the Registered Office of the company on Monday, the 12th March, 1952 at 4.30 P. M.

Present : Chairman.

..... }
 } Directors
 }

and 20 other members.

1. Notice of Meeting—The notice dated 15th Feb. 1952 convening the Meeting was read.

2. Statutory Report—The Chairman made an inaugural speech about the formation of the company and its prospectus, and then invited discussion and questions on the Statutory Report and matters relating to the formation of the company. The question put forward by the members having been answered, it was resolved on the motion of the Chairman seconded by Mr. that the Statutory Report of the Company be adopted.

3. Modification of contract—On the motion of the Chairman, seconded by Mr. it was resolved that the following modification in the contract dated between the company and the Vendors, Messrs. be approved :—

“The purchase price of Rs. 5,00,000 be paid as to Rs. 1,00,000 in fully paid shares of the company instead of Rs. 2,00,000 in cash and the balance in fully paid shares as originally agreed.”

4. Vote of Thanks—There being no other business before the meeting, the meeting terminated with a Vote of thanks to the Chairman.
Chairman.

Minutes of the ordinary general meeting :

Jiyajee Rao Cotton Mills Ltd.

MINUTES of the Thirty Second Annual General Meeting of the company, held at the Registered office of the company on the 18th July, 1952....., at four o'clock.

Present : Chairman.

..... }
 } Directors
 }

and 20 other members.

.....Company's auditor.

205. Notice of Meeting—The Secretary read the notice convening the meeting.

206. Adoption of Accounts—Upon the motion of the Chairman, seconded by Mr. it is resolved unanimously that the Thirty Second Annual Report and Accounts annexed thereto be received and adopted.

207. Declaration of Dividends—Resolved that a dividend of..... per cent, on the ordinary shares of the company for the year ended.....195..... be and is hereby declared, payable forthwith to all members entered on the register of members on.....195.....

208. Election of Directors—On the motion of Mr. seconded by Mr. it was resolved that the retiring director Mr. be and is hereby re-elected.

209. Appointment of Auditors—On the motion of Mr. seconded by Mr., it was resolved that Mr. of Messrs; be and is hereby re-elected auditor of the company, at a remuneration of Rs. p a.

210. Vote of Thanks—Upon the motion of Mr. seconded by Mr. a Vote of thanks was recorded unanimously to the directors.

.....Chairman.

Minutes of the extraordinary general meeting :

Jiyajee Rao Cotton Mills Ltd.

MINUTES of an *extraordinary general meeting* of the company, held at Birla House, Birla Nagar on the 12th March, 1953 at 4.30 P. M.

Present : Chairman.

.....	} Directors
.....	
.....	
.....	
and 25 other members	

211. Notice of the meeting—The Secretary read the notice convening the meeting.

212. Increase in capital—The Chairman explained that owing to the expansion of the Company's business it had become necessary to increase the Company's capital in order to provide further working capital. The chairman moved and Mr. seconded "that the capital of the company be increased to Rs..... by the creation and issue of.....new ordinary shares of Rs.....each." Resolved accordingly.

213. Vote of Thanks—The proceedings was concluded by a vote of thanks to the Chairman.

.....Chairman.

Minutes of a Board meeting :

Jiyajee Rao Cotton Mill's Ltd.

MINUTES of a meeting of the Directors held on the 5th day of August 1952, at the registered office of the company.

Present : Chairman.

.....
.....
.....
..... } Directors

..... Legal Advisor.

102. Minutes of previous meeting—Minutes of the meeting held on.....were read and signed by the Chairman.

103. Resignation of Mr It was resolved that the resignation dated.....of Mr., a director, be accepted with regret and take effect from this date. The Board, however, takes this opportunity of recording its appreciation of his services to the Company.

104. Filling of Casual Vacancy—Resolved that Mr. be appointed a director of the company in the place of Mr. (who has resigned) for the remainder of the period for which Mr. was elected viz., until the annual general meeting to be held in.....

105. Report of Transfer Committee—The Report of the Standing Transfer Committee of the board was considered. It showed that applications were received for the transfer of 250 shares from fifteen shareholders all of which except one from Mr. were accepted and the transfers were given due effect to. It was resolved that the said report be accepted.

106. Purchase of Additional Machinery—It was resolved that the managing agents' proposal for the purchase of.....machinery at an approximate cost of Rs. be approved and that they be authorised to place the necessary orders.

107. Investment of Reserve Fund—Resolved that a sum of Rs. 1,00,000 representing the Reserve Fund of the Company be invested in the 3% Victory Bonds 1957, and that the interest to be received therefrom be credited to the Reserve Fund.

108. Declaration of Interim Dividend—Resolved that an interim dividend at the rate of.....per share free of income tax

on 2000 shares of the company be declared on account of 1947 and that it be payable to those shareholders whose names stand in the Company's Register of Members as on 5th August 1952;

109. Appointment of a Committee—Resolved that a committee of the Board consisting of Messrs.....(with Mr. as the convener) be appointed to examine thoroughly the proposal of starting a retail branch of the company in East Punjab, and to report to the board before.....

.....Chairman.

SPECIMEN DIRECTORS' REPORT*

Standard coal company, limited directors' report :

To

The Shareholders,

Gentlemen,

We beg to submit the audited accounts for the half-year ended 31st Decem. 1940.

96,016 tons were raised and 100,374 tons despatched during the half-year, as against 112,594 tons raised and 107,763 tons despatched during the previous half-year.

Despatches to the Indian Iron and Steel Co. Ltd., were made in full throughout the half-year.

Sand-stowing :

Work is proceeding in connection with the erection of the Ropeway for the transport of sand from the Damodar river to the Colliery. It had been hoped to have this Ropeway in operation by Decem. 1940, but owing to unforeseen delays due to war conditions, it is now unlikely that the Ropeway will be working before the end of 1941.

It must also be mentioned that a considerable amount of consolidation work will need to be done before the introduction of sand-stowing can lead to increased output. The continuation of the present reduced level of output must, therefore, be expected so continue during 1941, and for some months thereafter. Further more mining difficulties being met in areas now in process of development may lead so further reduction in output.

* Directors' Report extracted from "Business Organisation" by Prof. R. R. Gupta—P ges 173—174,

Market :

The market remained quiet throughout the half-year, with a tendency to a fall in prices during the end of the period. The outlook for the coal industry owing to surplus production and shortage of freight is most unsettled.

Colliery :

The mines and machinery were maintained in good order.

Accounts :

Owing to the recent increase in the surcharge on income tax, it has proved necessary to provide in this year's accounts for additional taxation payable in respect of previous half-year's profits.

The Profit and Loss Account, after making provision for taxation, providing Rs. 23,187/-/6 for Depreciation, writing off Rs. 2,500/- from prospecting and including the sum of Rs. 7,362/14/3 brought forward from last half-year, shows an available balance of Rs. 44,605/10/1, which we propose to dispose of as follows :—

In paying a Dividend	@ 10%	Rs 40,000—0—0
	(Per annum)	
In carrying forward		Rs. 4,605—10—1
		Total Rs. 44,605—10—1

Directorate :

Mr. D. H. WILMER retires at this time, and being eligible offers himself for re-election.

Auditors :

M/S Price Waterhouse Peat & Co., Chartered Accountants, the Auditors of the Company, retire, but offer their services for the ensuing year.

We are, Gentlemen,
Yours faithfully,

Calcutta,

Dated :

1.	} Directors.
2.	
3.	
4.	

SPECIMEN OF A CHAIRMAN SPEECH

Annual General Meeting of
Dalmia Cement Co. Ltd.

Gentlemen,

"I welcome you to the Fourteenth Annual General Meeting of your Company. The balance sheet and profit and loss account with the Report of your Directors for the year ended 31st December, 1951, are in your hands. You will agree that the working results for the year under review have been satisfactory "

Five year plan :

"The Five-year Plan recently presented to the country has placed the cement industry high in the order of priorities of industrial development. The Plan anticipates additional demand for basic commodities like cement, as a result of the general development during the five-year period. Emphasis has been laid generally on the fuller utilisation of existing capacities and in respect of the cement industry, expansion of the capacity is also planned. The rated capacity and actual production of the industry according to the Planning Commission in the year 1950-51 have been 31.94 lakh tons and 26.92 lakh tons respectively and the target for expansion under the Plan is to attain by 1955-56 the rated capacity of 50.16 lakh tons and actual production of 45.60 lakh tons, involving an estimated investment of Rs. 15.4 crores. The cement industry has already registered a substantial increase in the production capacity and the rated capacity at present is approximately 40.25 lakh tons. Together with the rise in consumption of cement inside the country, it is estimated by the Planning Commission that the exports of cement will also increase from 30 lakhs ton a year."

"Under the five-year Plan, the initiative and responsibility for securing the necessary expansion over the bulk of the field industry rests with enterprise. The total capital investment needs for industrial expansion in private sector have been estimated at Rs. 233 crores, besides Rs. 150 crores required for replacement and modernisation of the existing plant capacity. The major question in this context is the availability of finance needed for development in the private sector.

Capital formation under the plan :

"The Plan appears to have overlooked to provide facility for capital formation. The recommendations of the Plan placing

restrictions on distribution of profits and issue of bonus shares, will further aggravate the difficulties of securing fresh capital. Such a policy is likely to make investment shy. Even the expectations of the Plan that new capital to the extent of Rs 90 crores would be available, may not materialise in the absence of any constructive and positive attitude towards."

"The main source of finance according to the Plan is the accumulation of undistributed profits of corporate industry which are estimated, exclusive of depreciation reserve, at Rs 200 crores. The quantum of undistributed profits is expected to increase by exercise of restraint in dividend policies and by enforcing agreed price increases in selected lines. Considering the depression which has overcome the market and the increasing competition which the industry is facing, it is unsafe to expect that the industries will earn such profits that these may be accumulated and ploughed back in adequate measure in expansion schemes.

Labour welfare schemes :

"Labour welfare schemes are good and they should be enforced, but the enormity of these schemes in such a short spell of time coupled with labour tribunals is giving a trying period to the industry. This strain on the industry can be substantially reduced if labour determines to improve efficiency and production. Otherwise, in the long run, both labour and capital are bound to suffer severely. The Plan accepts that the rate of progress has to be determined not only by the needs of workers but also by the limitations of the country's resources and that, too rapid changes or changes on a wide scale may result in financial, administrative and other difficulties which endanger new reforms and retard further development. It is, therefore, hoped that the Government will exercise care and caution and defer for at least the Plan period any new schemes likely to burden the industries with further expenditure.

"As already stated by me, the Plan has recommended agreed price increase in selected lines, as a means to increase the undistributed profits. While the recommendation is welcome and will be helpful, it may be pointed out that such increases can only be effected in respect of commodities which are under price control. Then there are also certain limitations upon the extent to which these increases can be sustained without affecting the consumption, which also has to be secured if the increased production is to be maintained.

Reduction in price of cement inopportune :

"Recent reduction in the controlled selling price of cement in India due to fall in prices of packing materials, has been inopportune and resulted in loss to the industry because of the large stocks of high-priced packing material held. The industry has represented to the Government regarding the increases in the production cost resulting from increased labour costs, compulsory statutory amenities, increase in raw material cost and transport freight, etc. The newly set up units and factories situated in the South are particularly hard hit. The Tariff Commission has now been entrusted with the fixation of fair selling price and all the cost increasing elements will be examined in detail by it. The industry is also placing before the Tariff Commission the need for making adequate reserves for replacement and modernisation of the old plant and equipment which has been subjected to heavy utilisation. In this connection the Plan has failed to envisage and has not made any recommendation for revision of the existing practise of allowing depreciation on the basis of original cost of the plant and equipment, even though the Plan has taken note of the high prices at which replacements have to be obtained, prices four times the original cost of the equipment. Thus, the industry is being taxed on the reserves needed for replacement which is against accepted principles of taxation besides being inequitable.

"It has also recommended the standardisation of wages in as large a field as possible. These measures, I am sure will be conducive to the attainment of an industrial truce which is necessary for achieving the targets of production.

"The Plan has also taken notice of the imperative need to reduce costs by rationalising industrial processes. A major difficulty in the way of increased production is the large surplus of labour which is on the pay-roll of industries. Assistance should be forthcoming in implementing schemes of rationalisation. Recently, we were compelled to discharge about 125 workers at Dalmiapuram factory, who had been taken in temporary employment for hand-packing of cement. They were employed on the clear understanding that they will be discharged as soon as the packing machine was installed. Now, even though the machine is ready to function, the workers oppose the discharge of these temporary workers and even resorted to a stay-in strike without any notice. If the workers'

unions are to serve the cause of labour in a sincere manner they should assist, rather than oppose any scheme of rationalisation. The Five year Plan has drawn pointed attention to the need for higher level of productivity and the responsibility of labour in achieving it. The Plan exhorts labour to accept greater regularity in attendance, disciplined behaviour and meticulous discharge of duties. I hope the workers of the country will act up to this advice and conduct themselves in a more responsible manner.

Industrial tribunals :

"There is general agreement that it is desirable to ensure avoidance of disputes by internal settlement, failing which voluntary arbitration may be accepted. The recommendation of the Plan regarding the recruitment and training of personnel of tribunals and the provision of technical help to them is welcome. Experience has shown that the existing tribunals manned by retired judicial personnel have been guided more by political thought than by the merits of the dispute in the adjudication proceedings. The personnel to be recruited and trained for the tribunals should be persons with sufficient insight into the problems of both labour and capital. If there are competent persons constituting the tribunals and they are kept free from executive interference and dependence the recommendation of the Plan limiting the right of appeals to exceptional cases, would be justified "

Plan should be made a success :

"Before I close my address, I would like to say that it is easy to find fault with any plan, but we must realise that with all its limitations it is the first planned effort towards the development of the country's resources and towards increasing the standard of living of our people and we must all strive hard and contribute our maximum effort towards the success of the Plan. It is the effort of each one of us which is needed to make our Five-year Plan a success. This Plan is the country's revolution. It is our ambition ; the outside world is going to judge us by our achievement in this sphere. The country's reputation and prestige are involved in it and so are our welfare and prosperity."

"In the end, I would like to express the Company's sincere appreciation of the services rendered by our workers and staff in different factories and offices.

"I now move that the balance-sheet and profit and loss account and the Directors' report for the year ended 31st. December, 1951, be approved and adopted by you."

DISTRIBUTION OF PROFITS AND DIVIDENDS

General provisions :

Dividends are the profits distributed to the shareholders either on a percentage basis or at a fixed sum per share on the issued capital of the company. In actual practice, the declaration and payment of dividends are determined by the articles. The articles generally provide that the dividends are to be recommended by the directors and sanctioned by the shareholders in general meeting. It is in fact the duty of the company secretary to carefully scrutinise the articles of the company in order that he might be able to guide the board of directors in chalking out a sound dividend policy. For the guidance of directors, he should prepare a statement showing what amounts will be observed at different rates on ordinary or deferred shares after paying fixed dividends on preference shares and also making provision for the creation of any reserves etc. according to the articles. In the declaration of dividends, Regulations 95 and 97 of Table A and the provisions of Section 107 are pertinent :—

(1) Regulation 95 of Table A provides that no dividend shall exceed the amount recommended by the directors.

(2) Regulation 97 of Table A which is also compulsory for all companies, provides that no dividend shall be paid otherwise than out of the profits of the year or any other undistributed profits. It means that no dividend can be paid out of capital.

(3) PAYMENT OF INTEREST OUT OF CAPITAL :—In special circumstances, however, mentioned in Section 107, if the shares are issued either

(i) to defray the expenses of construction of any works and buildings or,

(ii) for the provision of any plant which cannot be made profitable for a lengthened period,

(iii) the company may pay interest on capital out of capital and may charge the same to the cost of the works as capital expenditure subject to the following conditions :—

(i) the payment must be authorised by the articles or passed by a special resolution of the company.

(ii) the sanction of the Central Government to such payment must have been obtained.

(iii) the Central Government in such cases will appoint a person to enquire and report as to circumstances of the case ; the

cost of enquiry is to be paid by the company for which the Central Government may demand any security.

(iv) the period for which interest may be paid will be determined by the Central Government and will not extend beyond the close of half year next after the half year during which the works are completed.

(v) the rate of interest shall not exceed 4% and shall be determined by the Central Government.

(vi) rate of interest and the share capital on which interest is paid would be shown separately in the accounts of the company.

When interest is so paid out of capital the payment would not operate as reduction of capital. The above mentioned restrictions do not apply to companies governed by Indian Railways Companies Act, 1895 or the Indian Tramways Act, 1902.

(4) OTHER PROVISIONS :—The articles may also contain the following other provisions with regard to the distribution of profits . —

(a) The directors may pay interim dividends ;

(b) The dividends are declared and paid according to the amounts paid on shares, no dividends are to be paid upon calls paid in advance ;

(c) Directors may set aside out of the profits such amounts as they think proper as a reserve or reserves for meeting contingencies or for equalising dividends ;

(d) When a share or shares stand in the joint names of more than one holder, any one of them may give a receipt for dividends paid in respect of such shares and a receipt so given would be a valid discharge ;

(e) Notice of the dividend declared must be given to all the members in the manner prescribed by the company's regulations for giving notices ; and

(f) Dividends must be paid in cash or as otherwise provided by articles.

Dividend notices :

The dividends having been decided upon, the secretary should send a notice to the press regarding the dividends declared and the date on which it would be payable and requesting them to

notify immediately change of address if any. The following is a specimen of such a notice :—

Jiyajee Rao Cotton Mills. Ltd.

NOTICE IS HEREBY GIVEN that a meeting of Board of Directors of the above company held this day, an AD-INTERIM Dividend for the half year ended 30th sept. 1953, at the rate of Rs. 4, per fully paid share of Rs 50 - each (free of income tax) was declared. The dividend will be made payable on and after 15th Jan. 1953, to those shareholders whose names stand on the Register of the Company on 15th Decm. 1953, to whom dividend warrants shall be posted in due course.

The transfer books of the company will be closed from Friday, the 15 Dec. 1953 to Friday the 29th Dec. 1953, both days inclusive.

Shareholders are requested to notify immediately any change of the address to the undersigned.

Birla House,
Birla Nagar,
Gwalior 28th. Nov., 1953

By order of the Board,
Birla Bros. Ltd.
Managing Agents.

Dividend Mandates :

Those shareholders who wish that their dividends be paid to a bank for the credit of their account, may send a dividend mandate to the company in the following form :—

Place.....

Date.....

The Directors,
.....Company Ltd ,

Dear Sirs,

I request that you will, until further notice pay all dividends that may from time to time become due on any shares now standing or which may hereafter stand in the company's books in my name to....., whose receipt shall be your sufficient discharge.

Yours faithfully,

Dividend lists :

It is the duty of the company secretary to prepare dividend lists upon loose sheets (which may be bound up afterwards), in the following form the Register of Members. After the lists have been prepared they should also be carefully checked and totalled and made to agree with the total number of shares when dividend are paid on different classes of shares, separate lists should be prepared for each class.

Dividend warrants :

A dividend warrant is virtually a cheque on the authority of which the shareholders of a company receive payment of the dividends to which they are entitled. Dividend warrants are usually divided into two parts—the first part serves as a notice of the payment of the dividend and a voucher for the payment of income tax and the second or the lower part is a cheque for the payment and a receipt for such payment. The shareholders should keep the top part and detach and send the lower part, which is generally crossed to a bank. The following are the specimens of dividend warrants —

1. Dividend warrant 'directly payable by bank '

Jiyajee Rao Cotton Mills Ltd.

Birla House,
Birla Nagar, Gwalior
10th March, 1953

No. 250

DIVIDEND WARRANT for Rs. 50 (Rupees fifty only), being dividend at the rate of Rs 5 per share, for the year 1952, without deduction of income tax, on ten ordinary shares in the company standing in the name of, payable at the Company's Bank. This dividend was declared at the Thirty Second Ordinary General Meeting of the company held on Friday, the 2nd March, 1953.

We hereby certify that income-tax on the entire profits and gains of the company, of which this dividend forms a part, will be duly paid us to the Government of India.

Jiyajee Rao Cotton Mills Ltd.

.....
Managing Agents.

(To be signed by the claimant)

Dividend Warrant No 250.

I hereby certify that the dividend above mentioned relates to shares which were my own property at the time when the dividend was declared and were in possession of myself.

Date.....

Signature of claimant

CAUTION. The above certificate must be carefully preserved, as it will be required by the Income Tax Officer, when you claim refund of income tax on this dividend.

.....Perforation.....

Jiyajee Rao Cotton Mill's

Birla House,
Birla Nagar, Gwalior.
10th March, 1953.

Dividend Warrant No. 250.

To

The.....Bank, Ltd.,
Gwalior.

Pay to Mr.....or order the sum of Rupees fifty only
Rs. 50-.....

Payees Signature..... Managing Agents.

N. B. This draft must be signed by the payee and presented for payment within two months.

2. Dividend warrant payable at the company's office.

Jiyajee Rao Cotton Mills. Ltd.

Birla House,
Birla Nagar, Gwalior.
10th March, 1953.

No. 250

DIVIDEND WARRANT for Rs. 50 (Rupees fifty only), being dividend at the rate of Rs 10/- per share, for the year 1952, without deduction of income tax, on five ordinary shares in the company standing in the name of Mr...payable at the Registered Office of the company in Gwalior. This dividend was declared at the Thirty Second Ordinary General Meeting of the company held on Friday, the 2nd March, 1945.

We hereby certify that income tax on the entire profits and gains of the company, of which this dividend forms a part, will be duly paid by us to the Government of India.

Jiyajee Rao Cotton Mills Ltd.,

.....

Managing Agents.

(To be signed by the claimant)

Dividend Warrant No. 250.

I hereby certify that the dividend above mentioned relates to shares which were on my own property at the time when the dividend was declared and were in possession of myself.

Date.....

Signature of claimant

CAUTION : The above certificate must be carefully preserved as it will be required by the Income Tax Officer when you claim refund of income tax on this dividend.

.....Perforation.....

Jiyajee Rao Cotton Mills Ltd.

Dividend Warrant No. 250.

Received from the above named company 50/- (Rupees fifty only) being dividend payable on shares in Dividend Warrant No. 250 for the year, 1953.

Signature of Shareholder

Date.....

Witness.....

This formal receipt is being returned duly signed for payment. Please pay the amount at any cost by cheque, cash, money order or postal order.

Date.....

Signature of shareholder

Filing of return with I. T. O.

Under section 19 A of the Indian Income Tax Act, 1922, the secretary must send to the Income Tax Officer, a return stating the names and addresses of the shareholders of the company receiving dividends in excess of one rupee and also the names and addresses of those other shareholders who receive dividends exceeding Rs. 5,000/-. Separate forms must be used for resident and non-resident shareholders.

ISSUE OF BONUS SHARES

Some companies instead of paying high dividend or having built up large reserves from the profits of previous years, issue bonus shares. The objects of issuing such shares may be to—

(i) Bring the issued capital of the company in consonance with its present producing capacity, where the company is under-capitalised ; or

(ii) Keep the future dividends of the company within reasonable limits when its business and profits are steadily increasing.

Procedure of issue of bonus shares :

(1) First of all the company article may have to be altered by calling an extra-ordinary general meeting to pass special resolution with a view to take the necessary power (if it does not exist).

(2) Then on the recommendation of the directors, the company will pass an ordinary resolution in general meeting declaring the bonus to be satisfied by the allotment of Bonus shares. The following is a specimen of such a resolution :—

“That it is desirable to capitalise a sum of Rs....being part of the undivided profits of the company, and that the said sum of Rs.... be capitalised and that this amount be used as a capital bonus which shall be applied on behalf of the persons who are on the..... holders of..... issued ordinary shares of the company of.....each in payment full for.....additional shares of.....each and that such.....additional ordinary shares created as fully paid which shall rank for dividend and in all other respects *pari passu* with the issued ordinary shares of the company, shall be accordingly allotted to such persons respectively in the proportion of one of such.....additional ordinary shares for two of the said.....issued ordinary shares held on.....by such persons respectively, and that the additional ordinary shares so distributed shall be treated for all purposes as an increase of the nominal amount of the capital of the company held by each shareholder and not income.”

“That pursuant to the above resolution and in satisfaction of the said special capital bonus the directors be hereby directed to allot and distribute.....ordinary shares credited as fully paid amongst the persons who are on.....holders of the issued ordinary shares of the company in proportion to the issued ordinary shares held by them respectively with full powers to the directors to make such provision by the issue of fractional certificates or otherwise as they think expedient in the case of fractions.”

“That the draft of the agreement pending for the allotment of the said additional shares in satisfaction of the said capital bonus submitted to this meeting and signed in the margin by the chairman thereof by way of identification be approved and that the directors be authorised to affix the seal of the company to duplicate engrossment of such agreement as and when the same shall have been signed on behalf of the members holding ordinary shares in the company on.....by some persons to be appointed by the directors in that behalf.”

(3) Then the directors will nominate a shareholder to be a trustee for all the shareholders, and execute an agreement between

the company and the shareholders' trustee thereby constituting a right of the shareholders to the bonus shares.

(4) They will then make the allotment, provide for the adjustment of fractional parts of shares, authorise the issue of allotment letters and share certificates.

(5) It is the duty of the company secretary to file a return of allotment together with a copy of the contract showing the title of the allottees to the bonus shares, with the Registrar, and the necessary entries should be made in the books of the company.

(6) Where the company has issued its entire authorised capital, its authorised capital must be increased in accordance with the provisions of Section 50, before it can issue any bonus shares.

N. B. The Legal procedure in connection with the increase of share capital is discussed in the next chapter.

REORGANISATION RECONSTRUCTION AMALGAMATION ETC.

Reorganisation :

The term Reorganisation may be described as a new financial plan which replaces the old plan that has proved faulty. It is infact the process of tearing down the old financial structure of a company and using the materials in a new and stronger structure. It is a rearrangement of the company's liabilities. The objects of reorganisation may be :—

- (i) To simplify the capital structure with a view to raise further capital;
- (ii) To reduce fixed charges;
- (iii) To pay or to fund pressing obligation;
- (iv) To eliminate past losses; or
- (v) To take care of accumulated preference dividends.

Procedure of reorganisation :

Any scheme of reorganisation involving an arrangement between the company, its members, and/or its creditors, can be put through under section 153, an outline of which may be sketched as below :—

(1) On the application of any company, member, creditor or liquidator, the Court orders the holding of class meetings, as there may be Various classes of shareholders and creditors affected. The order of the Court also contains the procedure for the meeting and if the procedure is not laid down therein, the procedure of the articles is to be adopted.

(2) If, at the separate class meetings, the scheme is approved by a majority in number representing $\frac{3}{4}$ ths in Value of the members or the creditors voting in person or by proxy, it becomes binding on all members and creditors after it has been duly sanctioned by the Court and a copy of the Court's Order has been filed with the registrar.

*Note :—*An appeal lies against the order of the Court.

If the reorganisation scheme involves a reduction of capital under Section 55 or an alteration of capital under Section 50, it will be necessary to observe the provisions of those sections before the scheme can be sanctioned by the Court. (Those sections have already been discussed in details in Book I)

Reconstruction :

The term 'Reconstruction' stands for the formation of a new company to take over the assets of the old company with the object that substantially the same business shall be carried on by the same persons. Strictly speaking this term refers to the sale of the business of an existing company to another company which may be formed for the purpose. Reconstruction may be either for the purpose of raising its additional capital to expand its activities or to amalgamate with other company or companies. Other instances of reconstruction may be where a company may desire to make a compromise with its creditors offering them shares and debentures in the new company or where the object may be to readjust its share capital by writing off lost capital by an unsuccessful company or with a view to alter the objects or to change its constitution. The company under reconstruction has to go into voluntary liquidation by passing a special resolution.

Reconstruction of a company may be brought about in one of the following ways :—

(1) *By a sale under the memorandum followed by winding up*—The directors of a company, if the memorandum confers the necessary powers, sale or dispose of the undertaking with the consent of the company in general meeting (as required by Section 86 H); but the company must continue to its separate existence either as a holding company with the shares in the transferee company as its principal asset, or if the business is sold for cash, by investing the proceeds in the purchase of new assets. Such a scheme of reconstruction must provide for dissentient members of the transferor company and if it overlooks their rights, it ultravires the company.

(2) *By a sale and transfer of assets under Section 208 C*—A sale under Section 208 C becomes necessary when a company needs more capital, but cannot get it without putting some pressure on the existing shareholders. Under this section, reconstruction takes place on the following lines. The old company is transferred to a new company whether newly formed or an existing one. Infact the old company goes into liquidation and the liquidator of the transferor company may with the sanction of a special resolution receive in compensation shares etc. in the other company to distribute them among the members of the transferor company. Any such sale or arrangement shall be binding on the members of the transferor company.

If any member of a transferor company who did not Vote in favour of the special resolution, expresses his dissent therefrom in writing addressed to the Liquidator and left at the registered office of the company with in sevendays after the passing of the resolution, he may require the liquidator either to abstain from carrying the resolution into effect or to purchase his interest at a price to be determined by agreement or by arbitration. If the Liquidator elects to purchase the member's interest, the purchase money must be paid before the company is dissolved and be raised by the liquidator in such manner as may be determined by special resolution.

Under Section 209 F, the provisions of Section 208 (c) outlined above shall also apply in the case of a creditors' Voluntary Winding-Up as in the case of a Members' Voluntary Winding-Up, with the only modification that instead of a special resolution of the company, the scheme must be sanctioned by the Court or by the committee of Inspection.

(3) *Under section 153 and 153 A*, a reconstruction or amalgamation may also be affected under these sections but in such a case, the court may require the rights of dissentient shareholders to be properly protected in the same way as under section 208 C. According to these provisions, an application is made by the company itself, by any creditor or member of the company to the Court. The Court orders a meeting of the creditors or members as the case may be. If a three fourths majority in value present in person or by proxy, agree to the compromise or arrangement, it shall, if sanctioned by the Court, be binding on all the creditors and members and also on the company or its liquidators and contributories.

Moreover, the court may under section 153 A, make provisions for all or any of following matters :—

(i) The transfer to the transferee company of the undertaking and property or liabilities of any transferor company.

(ii) Alloting or appropriation by the transferee company of any shares, debentures, or other like interests in the company, which are to be allotted or appropriated by that company to or for any person.

(iii) The dissolution without winding up of any transferor company.

(iv) The continuation by or against the transferee company of any legal proceedings pending by or against any transferor company.

(v) The provision for any person who dissent from the compromise or arrangement.

AMALGAMATION

Amalgamation of companies is usually carried out with the object of eliminating destructive competition and effecting economies in production. It may be carried out in any of the following ways.—

(1) Under Section 153, 153 A and 208 C as already explained above.

(2) One company may purchase in the open market a sufficient number of shares of another company in order to give it a controlling interests in that company.

(3) Under section 153 B also, provision is made for the amalgamation of companies without the requirement of passing any resolution at meetings. According to this section, a company after consultation with its directors, makes an offer to the other company (known as transferee company) involving the transfer of shares of transferor company, which is approved with in four months after making the offer by the holders of three fourths in value of the shares affected. The transferee company gives notice with in two months to any dissenting shareholder that it desires to acquire its shares. The transferee company, with in a month from the date on which notice was given, is entitled to acquire these shares on the terms on which the shares of the approving shareholders are to be transferred.

INCREASE OF SHARE CAPITAL

The share capital of a company may be increased in any of the following two ways :—

(1) *By the Directors Issuing the Unissued Shares*—Section 105 C provides that, where the directors decide to increase the capital of the company by the issue of further shares, such share shall be offered to the members in proportion to the existing shares held by each member irrespective of class, and such offer shall be made by notice specifying the number of shares to which the member is entitled, and limiting a time within which the offer, if not accepted, will be deemed to be declined; and after the expiration of

such time, or on receipt of an intimation from the member to whom such notice is given that he declines to accept the shares offered, the directors may dispose of the same in such manner as they may deem most beneficial to the company. This is, in legal terminology, known as the shareholders' Right of Pre-emption.

Legal procedure :

(i) The directors should first pass a resolution offering the shares to the existing members, and authorise the issue of the necessary notice to be sent to the members specifying the number of shares to which the members is entitled and also specifying the date before which the offer may be accepted.

(ii) The share books of the company must be closed for some time by giving a public notice in order that the notices to the members may be drafted.

(iii) After the letter of acceptance is received from a member, the contract becomes complete and no formal allotment is legally necessary; but in actual practice a formal allotment is usually made by the directors.

(iv) The shares not taken up by the members should be disposed of by the directors at the best available prices.

(v) A return of allotment must also be filed with the Registrar.

(vi) Then after the secretary should prepare the necessary share certificates and arrange to send them to the members.

(vii) Necessary increase should also be made in the register of members.

(2) *By the Company increasing its authorised capital and creating new shares for issue*—It may be remarked at the outset that, in the absence of an express provision in the articles or in the absence of a resolution of the company, the existing shareholders have no right of pre-emption in regard to such new shares.

Legal procedure :

(i) The directors should first of all decide at their meeting that the authorised capital of the company should be increased.

(ii) The Secretary should then issue notices calling an extraordinary general meeting along with a circular explaining the need for the increase of capital.

(iii) At the general meeting, the necessary resolution will be passed authorising the increase of share capital. Such a resolution may be worded as follows :—

"That the capital of the company be increased to Rs. by the creation of new ordinary shares of Rs. each ranking for dividend and in all other respects *pari passu* with the existing ordinary shares in the company provided that such shares shall not participate in any dividend declared before..... 195....., in respect of profits accrued upto the.....195....., but shall participate in any dividend declared thereafter *pro rata* with the existing capital." "That the said.....new Ordinary Shares be offered in the first instance at a premium of Rs. per share to the ordinary shareholders of the company in proportion, as nearly as may be, to the number of ordinary shares held by them respectively, and such offer be made by notice specifying the number of shares to which the member is entitled and limiting a ¹⁴ ₁₅ within which the offer if not accepted will be deemed to be declined and that the Directors be empowered to dispose of the shares not taken response to such offer to such persons and upon such terms as they may deem expedient in the interests of the Company."

(iv) A notice of the increase of capital must also be given to the registrar within a fortnight from the date of the resolution, and the necessary capital duty should be paid.

(v) The share books of the company must be closed for some time by public advertisement in order that the notices to the members may be prepared.

(vi) The directors will then pass a resolution offering the new shares to the existing members, and authorise the issue of the necessary notice to be sent to the members specifying the number of shares to which the member is entitled and also specifying the date prior to which the offer is to be accepted.

(vii) After the letter of acceptance is received from a member, the contract becomes complete.

(viii) The shares not taken up by members, will be disposed of by the directors at the best available prices.

(ix) A return of allotment also be filed with the Registrar.

(x) The Secretary should then prepare the necessary share certificates in respect of the new shares and should arrange for their despatch to the members.

(xi) Necessary entries should also be made in the register of members.

Test & Examination Questions

1. What qualifications should the secretary of a joint stock company possess in order to perform his duties efficiently? (Agra M. Com. 1948).

2. Describe in detail the law and practice regarding the forfeiture of shares and the reissue of forfeited shares. (Agra M. Com. 1948).

3. What precautions should a company secretary take before issuing a duplicate share certificate in place of the one lost by a share holder. (Agra M. Com. 1947).

4. Describe briefly the secretarial practice relating to the transfer of a company's shares, and draft the notices that have to be issued to transferors and/or transferees. (Agra M. Com. 1945)

5. Distinguish between transfer and transmission of shares. What procedure is followed in each case? (Agra M. Com. 1947)

6. What statutory books and records are required to be kept in a company under the Indian Companies Act? (Agra M. Com. 1947)

7. Summarise briefly the provisions of the Indian Companies Act relating to a company's Register of Members. (Agra M. Com. 1945)

8. What is an annual return? What are its contents? (Agra M. Com. 1948)

9. What do you understand by a special resolution? How is such a resolution passed by a company? Draw up one supplying imaginary details. (Agra M. Com. 1947)

10. What is the legal provision for the holding of the ordinary general meeting of a company? What business is transacted at such meetings? What are the duties of a secretary in this connection. (Agra M. Com. 1948)

11. Draft notices for the following company meetings, giving the number of clear days' notice required in each case—(a) Statutory Meeting, (b) Meeting to alter the articles of association, and (c) Meeting to reduce the share capital. (Agra B. Com 1948)

12. What is the procedure to be followed at an annual general meeting of a joint stock company? Describe the duties of the secretary in connection with the meeting. (Bombay B. Com. 1942)

13. Draft imaginary minutes of the annual general meeting of a limited company (Alld. B. Com. 1940)

14. Distinguish between Statutory meeting, annual general meeting and extraordinary meeting of the shareholders of a company. (Alld. B. Com. 1937)

15. Write (a) a notice calling an extraordinary general meeting of a company for the purpose of altering its articles of association, if the meeting is to be held immediately after the ordinary general meeting convened on the same date, and (b) a circular to shareholders explaining the reason for such alteration. (Agra M. Com. 1945)

1 COMPANY SECRETARIAL PRACTICE

16. Outline the general rules of procedure at company meetings in relation to resolutions, amendments and voting. (Agra M. Com. 1945)
 17. What are the duties of a company secretary in connection with the meetings of its directors ? (Agra M. Com. 1946)
 18. Draw up the agenda and write out the minutes of the meeting of directors of a sugar mill company convened to consider and pass annual accounts of the company. (Agra M. Com. 1947)
 19. Describe briefly the secretarial practice relating to the payment of dividends by a company and draft the form of a dividend warrant with income tax certificate attached thereto. (Agra M. Com. 1945)
 20. What is the procedure to be adopted if a company wishes either (a) to increase its authorised capital or (b) to capitalise its profits ? Draft a complete resolution for the purpose (Agra M. Com. 1945)
 21. What is the scheme of arrangement under section 153 of the Indian Companies Act of 1913 ? Explain the scope of this section and outline the procedure. (Agra M. Com. 1945)
 22. Describe briefly the nature of a reconstruction scheme under section 208—C of the Indian Companies Act. (Agra M. Com. 1945)
 23. How and under what circumstances can a company reduce its share capital ? (Agra M. Com. 1947)
 24. A shareholder writes inquiring how the company is progressing and if there is any likelihood of an increased dividend being paid this year. He adds that he is thinking of buying a few more shares and he would like to know if you would advise him to do so. Write an appropriate reply. (Agra M. Com. 1951)
 25. Draft the statement in the Directors' Report of a company, which deals with the disposal of profits, supplying details from imagination. (Agra M. Com. 1951)
 26. Describe fully the procedure adopted for issuing bonus shares. Draft a resolution to capitalize a part of the undivided profits. (Agra M. Com. 1952)
 27. Draft a short speech to be delivered by the chairman at the annual general meeting of a company manufacturing cotton cloth, reviewing the general problems facing the industry and stressing the need for stable and long term policy on control measures. (Agra M. Com. 1952)
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